MICHAEL DONOFRIO
(802) 858-4465
(802) 342-4794 (fax)
michael.donofrio@strismaher.com
Admitted in New York and Vermont

July 30, 2019

VIA ELECTRONIC MAIL

Michael Barber
Green Mountain Care Board
144 State Street
Montpelier, VT 05602

Re: **Blue Cross and Blue Shield of Vermont Small Group & Individual 2020 VHC Rate Filing (Docket no. GMCB-006-19rr); Rate Hearing Follow Ups**

Dear Mr. Barber,

Below please find BCBSVT's responses to the questions posed by the Board at the July 23, 2019 hearing and set forth in your letter of July 24, 2019. These responses will not be filed in SERFF.

1. **Please provide a breakdown of *unit cost* increases in the following provider categories: (1) GMCB regulated entities; (2) non-GMCB-regulated, direct BCBSVT contract entities; and (3) entities that contract with other Blue entities.**

   BCBSVT Response: The table below includes the corrected unit cost increases provided in our response to inquiry 1, the impact of the recently submitted Vermont hospital budgets, and finalized contracts with NH hospitals. It is consistent with the information provided on Hearing Exhibit 18.

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Annual Reimbursement Changes due to Budget Increases and Contracting Season	Percent of Total Allowed Medical Claims in Experience	Cost Trend from 2018 to 2019	Cost Trend from 2019 to 2020	Total Annual Cost Trend
Vermont facilities and providers impacted by GMCB's Hospital Budget Review	51.1%	2.8%	4.3%	3.5%
Facilities and provides that BCBSVT contracts directly with but outside of the GMCB Hospital Budget Review	34.1%	1.3%	2.2%	1.6%
Other facilities and providers	14.8%	3.4%	3.6%	3.5%
Total	100.0%	2.3%	3.5%	2.89%

2. **If possible, provide a breakdown of *utilization* in the provider categories described in the immediately preceding question. If this is not possible, explain why it is not possible.**

   BCBSVT Response: BCBSVT does not project the utilization trend by the provider categories in question 1. Instead, we look at the different types of services regardless of the place of service for our analysis. That said, we can observe the historical utilization and intensity trend by those categories. Using the same population underlying the data in Exhibit 3B of our filing, we experience the following historical trends:

Annual Increase	VT / GMCB	Direct Contract	Other	Total
CY2016 / CY2015	2.0%	-2.3%	6.0%	1.1%
CY2017 / CY2016	0.7%	11.7%	-5.5%	3.4%
CY2018 / CY2017	0.1%	4.1%	27.6%	4.8%

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3. **Please provide a crosswalk comparing the administrative costs discussed in HCA Exhibit 21, page 21, with those identified in BCBSVT Exhibit 1, page 52.**

   BCBSVT Response: Please see Attachment 1 for the crosswalk of administrative expenses reported in the BCBSVT rate filing (BCBSVT Exhibit 1, page 52) to those reported in the Underwriting and Investment Exhibit, Part 3 (U&I – Part 3) of the annual statutory filing (HCA Exhibit 21, page 21). Note that the expenses identified in the rate filing are reported in accordance with U.S. Generally Accepted Accounting Principles (GAAP), while the expenses in U&I – Part 3 are reported in conformity with statutory accounting practices of the National Association of Insurance Commissioners' (NAIC) Accounting Practices and Procedures manual (NAIC SAP). NAIC SAP is a comprehensive basis of accounting other than GAAP that is required to be used by the insurance industry. As of January 1, 2001, the State of Vermont Department of Financial Regulation (DFR) adopted NAIC SAP as the basis for statutory accounting practices in the State of Vermont, pursuant to 8 V.S.A. §3561.

   While the underlying expenses are virtually the same, the presentation of the expenses under NAIC SAP differs in many ways from that of GAAP. The differences that are applicable to BCBSVT's expense reporting are described in the explanation column of Attachment 1.

4. **Regarding administrative costs reflected in HCA Exhibit 21, page 21, please provide additional explanation regarding the PMPM allocation of costs between BCBSVT's insured and ASO businesses.**

   BCBSVT Response: BCBSVT's cost allocation process is designed and operated for the purpose of distributing administrative expenses across each of BCBSVT's market segments based on the relative proportion in which each segment drives or benefits from those expenses. At a high level, the process requires each cost center to be reviewed by cost accounting staff in order to determine the most appropriate allocation methodology for that cost center's expenses. The cost accounting team interviews the cost center manager in order to understand the functions and activities performed by personnel in that cost center, their processes for completing those functions, and what factors drive the amount of work the personnel put into each market segment. Based on that information and with input from the cost center manager, an expense allocation methodology is developed that most fairly and accurately represents the proportionate work effort that the cost center contributes to each market segment. The same exercise is used to allocate expenses that are not related to BCBSVT personnel effort, such as external vendor costs, regulatory fees, etc.

   Allocation methodologies are typically based on statistical metrics, such as number of members, number of claims submitted or processed, number of inquiries or cases, number of groups, etc. For example, the claims processing department expenses may be allocated based

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on the number of claims that are processed for each market segment. Expenses in the customer service department may be allocated based on the number of phone inquiries received from each market segment. A cost center may have multiple metrics or other allocation rules combined, depending on the functions performed and the types of costs incurred.

As the end result of this process, some market segments are allocated proportionately more expenses per member than other segments. Simply put, this is because some segments cause BCBSVT to incur more expenses relative to their membership than others. Individual business is generally more costly to administer than large group, for many reasons. First, direct contact with each subscriber is required in the individual market; for large group, direct communication is typically only with one point of contact at each group. Additionally, many large groups are able to provide information to BCBSVT via electronic, automated processes, while individuals usually have to be processed manually, one at a time.

Specifically to the question about allocation of costs to BCBSVT's insured and ASO business segments, there are several factors causing insured business to incur a proportionately higher administrative cost PMPM than ASO. These include, but are not limited to, the following:

- Group size – the ASO segment comprises BCBSVT's largest group customers, and as such, requires significantly less manual effort and systems cost per member than the insured segment, which is made up of VISG and a few smaller "large" groups that purchase insured products.
- ACA and other regulatory fees – many fees assessed as a result of the ACA, most notably the health insurer tax (HIT), are not applicable to ASO plans. The HIT fee, which is by far the largest assessment incurred by BCBSVT, is based strictly on insured premium written and can only be recovered from insured groups. In the years that it is in effect, the HIT fee alone can nearly double the PMPM cost of insured business as compared to ASO.
- Demographics – BCBSVT's insured business, primarily driven by the individual portion of VISG, is an older and generally less healthy population than the ASO segment. As a result, it creates more claims to be processed, more calls and other inquiries, and overall more expenses to administer.

BCBSVT regularly compares its PMPM costs by market segment to industry benchmarks to see if they appear reasonable relative to other health insurers. One such benchmark is published by the Sherlock Company, which performs annual studies of administrative expenses in a variety of health insurance markets, including Blue Cross Blue Shield

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Plans. Sherlock recently published the summary results of their study of 2018 Blue Plan administrative expenses in the June 2019 "Plan Management Navigator. [1]" On page 8 of this document, Figure 4 shows the median, 25th percentile, and 75th percentile values of PMPM costs by market segment for the 14 Blue Plans (collectively serving 36.7 million members) that participated in the study (BCBSVT did not participate, although it has in past years). The results show a consistent pattern with what BCBSVT has experienced, which is that insured products are more costly to administer per member than ASO. With the HIT fee being in effect in 2018, it is not surprising that the median administrative expense PMPM across a large section of the Blues system was significantly higher for insured business than for ASO.

For comparison purposes, note that BCBSVT's VISG business would fall in the category of "Commercial Insured." In 2018, the median administrative expense PMPM for that category in the Sherlock study was $49.84, which compares to BCBSVT's actual 2018 experience of $44.96 PMPM and filed 2020 administrative charge of $46.12 PMPM[2].

5. **Provide the relevant portions of the Statutory Accounting Principles referred by Ms. Greene in her testimony concerning the following statement in BCBSVT Exhibit 10: "Under this formula, BCBSVT was required to non-admit, or remove from reserves, $13.3 million of the DTA balance attributable to AMT credits."**

BCBSVT Response: As described in the response to question 3, BCBSVT's financial reporting must be prepared in conformity with statutory accounting practices of the National Association of Insurance Commissioners' (NAIC) Accounting Practices and Procedures manual (NAIC SAP). As of the 2018 manual, NAIC SAP guidance includes 107 Statements of Statutory Accounting Principles (SSAPs) and 8 appendices, which include "Issue Papers" and various other documents providing interpretations of the guidance outlined in the SSAPs.

Attachment 2 is a copy of SSAP No. 101, *Income Taxes*. This document provides the NAIC SAP guidance for accounting and reporting of income taxes, both current and deferred, as well as admissibility of income tax assets. Beginning on the fifth page of Attachment 2, paragraphs 9 – 12 of SSAP No. 101 set forth the requirements and methodology for determining the amount of deferred tax assets (DTAs) that may be "admitted" (included in both assets and reserves) by an insurer in any particular reporting period. BCBSVT followed this guidance in calculating the $13.3 million portion of its DTA balance that was required to be non-admitted under SSAP No. 101 as of December 31, 2017, per the referenced language in BCBSVT Exhibit 10. In accordance with paragraph 11(b) of SSAP No. 101, BCBSVT

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[1] https://sherlockco.com/docs/navigator/June2019/Blue%20June%20Navigator%202019.pdf
[2] BCBSVT 2020 VISG Actuarial Memorandum, page 42 (Binder Exhibit 1, page 52)

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was allowed to admit the maximum DTA balance of 15 percent of reserves due to its RBC being greater than 300 percent, based on the reserve balance excluding the impact of DTAs and electronic data processing (EDP) equipment. The calculations of admitted and non-admitted DTA balances as of both December 31, 2018 and 2017 are shown in the table below:

	As of December 31,	
Admitted income tax asset calculation:	2018	2017
Reported NAIC SAP reserves per annual statement (page 3, line 33, column 3)	$ 110,154,828	$ 134,053,991
Total deferred tax asset (DTA) balance (page 2, line 18.2, column 1)	35,789,384	33,219,931
NAIC SAP reserves prior to application of DTA admissibility test	$ 145,944,212	$ 167,273,922
Deduct:		
Electronic data processing (EDP) equipment (page 2, line 20, column 3)	(1,419,629)	(1,491,699)
DTA balance	(35,789,384)	(33,219,931)
NAIC SAP reserve balance used for limitation calculation (SSAP No. 101, par. 11(b)(ii))	$ 108,735,199	$ 132,562,292
Realization threshold limitation percentage (SSAP No. 101, paragraph 11(b))	15%	15%
Admitted DTA asset limitation	$ 16,310,280	$ 19,884,344
Non-admitted DTA calculation:		
Total DTA balance	$ 35,789,384	$ 33,219,931
Deduct: Admitted DTA asset limitation*	(16,310,280)	(19,884,344)
Portion of DTA balance to be non-admitted	$ 19,479,104	$ 13,335,587

* Non-admitted in conjunction with permitted practice approved by DFR

6. **Describe whether BCBSVT considers how differences in cost sharing for procedures like colonoscopies (i.e., procedures that can be charged as "screening" but also as "diagnostic" if done following positive results, for example, from a Cologuard© test) may result in providers recommending a high cost procedure for a screening rather than a lower cost screening option.**

   BCBSVT Response: BCBSVT continually considers benefit design within the context of reducing overall health care costs, as well as incentivizing members to seek out the most cost effective and highest quality care. At the hearing, it appears there may have been some confusion about whether or not Cologuard would be subject to zero cost share as a federally defined preventive service. Cologuard is eligible for zero cost share. If clinically indicated, after conducting the Cologuard test, providers may also perform a colonoscopy as a screening procedure in follow-up. The follow-up colonoscopy claim, if the claim is submitted with the screening diagnosis, will also be subject to zero cost share.

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It may be important to note that as related to preventive benefits, the United States Preventive Services Task Force determines which services are subject to zero cost share. (Note that federal rules pertaining to HDHP limit BCBSVT's ability to cover certain things at zero cost share for these types of plans.) The USPSTF conducts rigorous review of existing peer-reviewed evidence to determine potential benefits and harms related to preventive services. Services that receive a grade of A or B from the USPSTF are required to be provided by ACA compliant plans at zero cost share. The USPSTF routinely updates its list of eligible services and BCBSVT actively monitors that process.

Please contact me if you have any questions about the above.

Sincerely,

/s/ Michael Donofrio
Michael Donofrio

cc (by e-mail):

Rebecca Heintz (heintzr@bcbsvt.com)
Bridget Asay (bridget.asay@strismaher.com)
Kaili Kuiper (KKuiper@vtlegalaid.org)
Eric Schultheis (ESchultheis@vtlegalaid.org)
Jay Angoff (jay.angoff@findjustice.com)
Michael Barber (Michael.Barber@vermont.gov)
Thomas Crompton (Thomas.Crompton@vermont.gov)
Christina McLaughlin (Christina.McLaughlin@vermont.gov)

Attachment 1

BLUE CROSS AND BLUE SHIELD OF VERMONT
2020 VERMONT INDIVIDUAL AND SMALL GROUP RATE FILING

Responses to BCBSVT 2020 VISG Hearing Follow Ups

Administrative Expense Crosswalk
For the Year Ended December 31, 2018

	Reconciling Items	Explanation
BCBSVT GAAP Basis Administrative Expenses Per Rate Filing (BCBSVT Exhibit 1, Page 52)	**$ 79,712,766**	
Less:		
Administrative Expenses Allocated to HMO Subsidiary	(5,158,127)	Gross BCBSVT costs included in rate filing exhibit to calculate overall admin expense trend; amounts are not charged to VISG
Administrative Expenses Allocated to TPA Subsidiary	(3,206,211)	Gross BCBSVT costs included in rate filing exhibit to calculate overall admin expense trend; amounts are not charged to VISG
Net BCBSVT GAAP Basis Administrative Expenses	$ 71,348,428	
Plus:		
ACA/SoV Healthcare Fees and Assessments	13,000,633	Excluded from base admin expense in rate filing; charged as separate rate component
Broker Commissions	2,248,737	Excluded from base admin expense in rate filing; not applicable to VISG market
Total BCBSVT GAAP Basis Administrative Expenses	$ 86,597,798	
GAAP Basis to NAIC SAP Basis Adjustments:		
Administrative Fees from Self-Funded Plans	(33,439,917)	Self-funded admin fees are reported as an offset to admin expense in NAIC SAP; reported as revenue in GAAP
Depreciation Expense on Real Estate	(555,009)	Real estate depreciation reported as admin expense in GAAP; reported as offset to investment income in NAIC SAP
Imputed Rent Expense for Home Office	1,386,000	In NAIC SAP, rent expense is imputed on owned home office and reported as admin expense; GAAP has no such concept
Pension Expense	(862,368)	GAAP and NAIC SAP vary in their treatment of actuarial assumptions used in calculating net periodic pension expense
ITS Home Expenses	4,219,880	Fees paid to Host Blue Plans are reported as claims expense in GAAP; reported as admin expense in NAIC SAP
Other	(140,416)	Miscellaneous items that are required to be reported differently under GAAP vs. NAIC SAP
Net GAAP Basis to NAIC SAP Basis Adjustments	(29,391,830)	
BCBSVT NAIC SAP Basis Administrative Expenses Per Statutory Reporting (HCA Exhibit 21, Page 21)	**$ 57,205,968**	(Sum of line 26, columns 1 - 3)

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 138—Fair Value Measurements*
- *Issue Paper No. 157—Use of Net Asset Value*

SSAP No. 101
Income Taxes

STATUS

Type of Issue:	Common Area
Issued:	August 31, 2011
Effective Date:	January 1, 2012
Affects:	Supersedes SSAP No. 10 and SSAP No. 10R; Nullifies INT 00-21, INT (INT 01-19 and INT 01-20
Affected by:	No other pronouncements
Interpreted by:	INT 01-18, INT 06-12
Relevant Appendix A Guidance:	None

STATUS

SCOPE OF STATEMENT

SUMMARY CONCLUSION

Current Income Taxes

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Deferred Income Taxes

Admissibility of Income Tax Assets

Realization Threshold Limitation Table – RBC Reporting Entities

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Realization Threshold Limitation Table – Other Non-RBC Reporting Entities

Realization of Tax Benefits and Tax-Planning Strategies

Intercompany Income Tax Transactions

Intraperiod Tax Allocation

Interim Periods

Disclosures

Relevant Literature

Effective Date and Transition

REFERENCES

Relevant Issue Papers

EXHIBIT A – IMPLEMENTATION QUESTIONS AND ANSWERS

Income Taxes

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for current and deferred federal and foreign income taxes and current state income taxes. This statement supersedes conclusions reached in *SSAP No. 10—Income Taxes* and *SSAP No. 10R—Income Taxes, A Temporary Replacement of SSAP No. 10*.

SUMMARY CONCLUSION

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2. For purposes of accounting for federal and foreign income taxes, reporting entities shall adopt *FASB Statement No. 109, Accounting for Income Taxes* (FAS 109) with modifications for state income taxes, the realization criteria for deferred tax assets, and the recording of the impact of changes in deferred tax balances. One objective of accounting for income taxes is to recognize the estimated amount of taxes payable or refundable for the current year as a tax liability or asset. A second objective is to recognize deferred tax liabilities and assets for the future tax consequences of events that have been recognized in a reporting entity's statutory financial statements or tax returns. However, the second objective is realistically constrained because (a) the tax payment or refund that results from a particular tax return is a joint result of all the items included in that return, (b) taxes that will be paid or refunded in future years are the joint result of events of the current or prior years and events of future years, and (c) information available about the future is limited. As a result, financial statements will recognize current and deferred income tax assets and liabilities in accordance with the provisions of this statement based upon estimates and approximations. For purposes of this statement, only adjusted gross deferred tax assets that are more likely than not (a likelihood of more than 50 percent) to be realized shall be considered in determining admitted adjusted gross deferred tax assets.

Current Income Taxes

3. "Income taxes incurred" shall include current income taxes, the amount of federal and foreign income taxes paid (recovered) or payable (recoverable) for the current year. Current income taxes are defined as:

a. Current year estimates (including quarterly estimates) of federal and foreign income taxes payable or refundable, based on tax returns for the current and prior years, except as addressed in paragraph 3.b., and tax loss contingencies (including related interest and penalties) for current and all prior years, computed in accordance with *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* (SSAP No. 5R) with the following modifications:

   i. The term "probable" as used in SSAP No. 5R shall be replaced by the term "more likely than not (a likelihood of more than 50 percent)" for federal and foreign income tax loss contingencies only.

   ii. For purposes of the determination of a federal and foreign income tax loss contingency, it shall be presumed that the reporting entity will be examined by the relevant taxing authority that has full knowledge of all relevant information.

   iii. If the estimated tax loss contingency is greater than 50% of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% of the original tax benefit recognized.

b. Amounts incurred or received during the current year relating to prior periods, to the extent not previously provided, as such amounts are deemed to be changes in accounting

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estimates as defined in *SSAP No. 3—Accounting Changes and Corrections of Errors* (SSAP No. 3).

c. In determining when tax loss contingencies associated with temporary differences should be included in current income taxes under paragraph 3.a., and therefore included in deferred taxes under paragraph 7, a reporting entity is not required to "gross-up" its current and deferred taxes until such time as an event has occurred that would cause a re-evaluation of the contingency and its probability of assessment, e.g., the IRS has identified the item as one which may be adjusted upon audit. Such an event could be the reporting entity's (or its affiliate or parent in a consolidated income tax return) receipt of a Form 5701, Proposed Audit Adjustment, or could occur earlier upon receipt of an Information Document Request. At such time, the company must reassess the probability of an adjustment, reasonably re-estimate the amount of tax contingency as determined in accordance with paragraph 3.a., make any necessary adjustment to deferred taxes, and re-determine the admissibility of any adjusted gross deferred tax asset as provided in paragraph 11.

4. State taxes (including premium, income and franchise taxes) shall be computed in accordance with SSAP No. 5R and shall be limited to (a) taxes due as a result of the current year's taxable basis calculated in accordance with state laws and regulations and (b) amounts incurred or received during the current year relating to prior periods, to the extent not previously provided as such amounts are deemed to be changes in accounting estimates. Property and casualty insurance companies shall report state taxes as other underwriting expenses under the caption "Taxes, licenses, and fees." Life and accident and health insurance companies shall report such amounts as general expenses under the caption "Insurance taxes, licenses, and fees, excluding federal income taxes." Other health entities shall report such amounts as general administration expenses under the caption "Taxes, licenses, and fees." State tax recoverables that are reasonably expected to be recovered in a subsequent accounting period are admitted assets. State taxes are reasonably expected to be recovered if the refund is attributable to overpayment of estimated tax payments, errors, carrybacks, or items for which the reporting entity has authority to recover under a state regulation or statute.

Deferred Income Taxes

5. Because tax laws and statutory accounting principles differ in their recognition and measurement of assets, liabilities, equity, revenues, expenses, gains, and losses, differences arise between:

a. The amount of taxable income and pretax statutory financial income for a year, and

b. The tax bases of assets or liabilities and their reported amounts in statutory financial statements.

6. A reporting entity's balance sheet shall include deferred income tax assets (DTAs) and liabilities (DTLs) related to the estimated future tax consequences of temporary differences and carryforwards,

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generated by statutory accounting, as defined in paragraph 11 of FAS 109.

7. A reporting entity's deferred tax assets and liabilities are computed as follows:

a. Temporary differences are identified and measured using a "balance sheet" approach whereby statutory and tax basis balance sheets are compared;

b. Temporary differences include unrealized gains and losses and nonadmitted assets but do not include asset valuation reserve (AVR), interest maintenance reserve (IMR), Schedule F penalties and, in the case of a mortgage guaranty insurer, amounts attributable to its statutory contingency reserve to the extent that "tax and loss" bonds have been purchased;

c. Total DTAs and DTLs are computed using enacted tax rates;

d. A DTL is not recognized for amounts described in paragraph 31 of FAS 109; and

e. Gross DTAs are reduced by a statutory valuation allowance adjustment if, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50 percent) that some portion or all of the gross DTAs will not be realized. The statutory valuation allowance adjustment[1(146)], determined in a manner consistent with paragraphs 20-25 of FAS 109[2(147)], shall reduce the gross DTAs to the amount that is more likely than not to be realized (the adjusted gross deferred tax assets).

8. Changes in DTAs and DTLs, including changes attributable to changes in tax rates and changes in tax status, if any, shall be recognized as a separate component of gains and losses in unassigned funds (surplus). Admitted adjusted gross DTAs and DTLs shall be offset and presented as a single amount on the statement of financial position.

Admissibility of Income Tax Assets

9. Current income tax recoverables shall include all current income taxes, including interest, reasonably expected to be recovered in a subsequent accounting period, whether or not a return or claim has been filed with the taxing authorities. Current income tax recoverables are reasonably expected to be recovered if the refund is attributable to overpayment of estimated tax payments, errors, carrybacks, as defined in paragraph 289 of FAS 109, or items for which the reporting entity has substantial authority, as that term is defined in Federal Income Tax Regulations.[INT 06-12]

10. Current income tax recoverables meet the definition of assets as specified in *SSAP No. 4—Assets and Nonadmitted Assets* and are admitted assets to the extent they conform to the requirements of this statement.

11. The net admitted DTA shall not exceed the excess of the adjusted gross DTA, as determined under paragraph 7.e., over gross DTL. Adjusted gross DTAs shall be admitted based upon the

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three-component admission calculation at an amount equal to the sum of paragraphs 11.a., 11.b., and 11.c.:

a. Federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, including any amounts established in accordance with the provision of SSAP No. 5R as described in paragraph 3.a. of this statement related to those periods.

b. If the reporting entity is subject to risk-based capital requirements or is required to file a Risk-Based Capital Report with the domiciliary state, the reporting entity shall use the *Realization Threshold Limitation Table – RBC Reporting Entities* (RBC Reporting Entity Table) in this component of the admission calculation. The RBC Reporting Entity Table's threshold limitations are contingent upon the ExDTA ACL RBC Ratio[3(148)].

If the reporting entity is either a mortgage guaranty insurer or financial guaranty insurer that is not subject to risk-based capital requirements and is not required to file a Risk-Based Capital Report with the domiciliary state and the reporting entity meets the minimum capital and reserve requirements for the state of domicile, then the reporting entity shall use the *Realization Threshold Limitation Table – Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entities* (Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table) in this component of the admission calculation. The Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table's threshold limitations are contingent upon the following ratio: the numerator is equal to the sum of 1) surplus to policyholders, 2) less the amount of the admitted DTA in paragraph 11.a. (ExDTA Surplus) plus, 3) contingency reserves. The denominator is equal to the required amount of minimum aggregate capital required to be maintained under the applicable NAIC model law or state variation thereof based on the risk characteristics and the amount of insurance in force (Required Aggregate Risk Capital)[4(149)].

If the reporting entity (1) is not subject to risk-based capital requirements, (2) is not required to file a Risk-Based Capital Report with the domiciliary state, (3) is not a mortgage guaranty or financial guaranty insurer, and (4) meets the minimum capital and reserve requirements, then the reporting entity shall use the *Realization Threshold Limitation Table – Other Non-RBC Reporting Entities* (Other Non-RBC Reporting Entity Table). The Other Non-RBC Reporting Entity Table's threshold limitations are contingent upon the ratio of adjusted gross DTA (Adjusted gross DTA less the amount of DTA admitted in paragraph 11.a.) to adjusted capital and surplus[5(150)].

Realization Threshold Limitation Table – RBC Reporting Entities

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ExDTA ACL RBC (%)	11.b.i.	11.b.ii.
Greater than 300%	3 years	15%
200 – 300%	1 year	10%
Less than 200%	0 years	0%

Realization Threshold Limitation Table – Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entities

(See paragraph 11.b.) Ex DTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital (%)	11.b.i.	11.b.ii.
Greater than 115%	3 years	15%
100% to 115%	1 year	10%
Less than 100%	0 years	0%

Realization Threshold Limitation Table – Other Non-RBC Reporting Entities

Adjusted Gross DTA / Adjusted Capital & Surplus (%)	11.b.i.	11.b.ii.
Less than 50%	3 years	15%
50% to 75%	1 year	10%
Greater than 75%	0 years	0%

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The reporting entity shall admit:

i. The amount of adjusted gross DTAs, after the application of paragraph 11.a., expected to be realized within the applicable period (refer to the 11.b.i. column of the applicable Realization Threshold Limitation Table above; the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) following the balance sheet date limited to the amount determined in paragraph 11.b.ii.

ii. An amount that is no greater than the applicable percentage (refer to the 11.b.ii. column of the applicable Realization Threshold Limitation Table above: the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) of statutory capital and surplus as required to be shown on the statutory balance sheet of the reporting entity for the current reporting period's statement filed with the domiciliary state commissioner adjusted to exclude any net DTAs, EDP equipment and operating system software and any net positive goodwill.[INT 01-18] For financial guaranty or mortgage guaranty non-RBC reporting entities, the amount of statutory capital and surplus utilized for this part of the calculation does not include contingency reserves.

c. The amount of adjusted gross DTAs, after application of paragraphs 11.a. and 11.b., that can be offset against existing gross DTLs. The reporting entity shall consider the character (i.e., ordinary versus capital) of the DTAs and DTLs such that offsetting would be permitted in the tax return under existing enacted federal income tax laws and regulations. Additionally, for purposes of this component, the reporting entity shall consider the reversal patterns of temporary differences; however, this consideration does not require scheduling beyond that required in paragraph 7.e.

12. In computing a reporting entity's admitted adjusted gross DTA pursuant to paragraph 11;

a. For purposes of paragraph 11.a., existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, shall be determined in accordance with paragraphs 228 and 229 of FAS 109;

b. In determining the amount of federal income taxes that can be recovered through loss carrybacks, the amount and character (i.e., ordinary versus capital) of the loss carrybacks and the impact, if any, of the Alternative Minimum Tax shall be determined in accordance with the provisions of the Internal Revenue Code, and regulations thereunder;

c. The amount of carryback potential that may be considered in calculating the admitted

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adjusted gross DTAs of a reporting entity in paragraph 11.a. that files a consolidated income tax return with one or more affiliates, may not exceed the amount that the reporting entity could reasonably expect to have refunded by its parent; and

d. The phrases "reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years," "realized within one year of the balance sheet date" and "realized within three years of the balance sheet date" are intended to accommodate interim reporting dates and reporting entities that file on an other than calendar year basis for federal income tax purposes.

Realization of Tax Benefits and Tax-Planning Strategies

13. Future realization of the tax benefit of an existing deductible temporary difference or carryforward ultimately depends on the existence of sufficient taxable income of the appropriate character (for example, ordinary income or capital gain) within the carryback, carryforward period available under the tax law. The following four possible sources of taxable income may be available under the tax law to realize a tax benefit for deductible temporary differences and carryforwards:

a. Future reversals of existing taxable temporary differences

b. Future taxable income exclusive of reversing temporary differences and carryforwards

c. Taxable income in prior carryback year(s) if carryback is permitted under the tax law

d. Tax-planning strategies in paragraph 14 that would, if necessary, be implemented to, for example:

   i. Accelerate taxable amounts to utilize expiring carryforwards

   ii. Change the character of taxable or deductible amounts from ordinary income or loss to capital gain or loss

   iii. Switch from tax-exempt to taxable investments.

Evidence available about each of those possible sources of taxable income will vary for different tax jurisdictions and, and possibly, from year to year. To the extent evidence about one or more sources of taxable income is sufficient to support a conclusion that the reporting entity will realize the full or a partial amount of its adjusted gross deferred tax assets, other sources need not be considered. Consideration of each source is required, however, to determine the amount of the statutory valuation allowance adjustment that is recognized for gross deferred tax assets under paragraph 7.e.

14. In some circumstances, there are tax-planning strategies (including elections for tax purposes) that (a) are prudent and feasible, (b) a reporting entity ordinarily might not take, but would take to prevent an operating loss or tax credit carryforward from expiring unused, and (c) would result in

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realization of deferred tax assets. A reporting entity shall consider tax-planning strategies in determining the amount of the statutory valuation allowance adjustment necessary under paragraph 7.e. Consideration of tax planning strategies for the realization of deferred tax assets when determining admission under paragraph 11 is not required; however, such strategies shall not conflict with the tax planning strategies used when computing the statutory valuation allowance. Any significant potential expenses to implement a tax-planning strategy or any significant losses that would be recognized if that strategy were implemented (net of any recognizable tax benefits associated with those expenses or losses) shall reduce the amount of admission under paragraph 11.

15. When a prudent and feasible tax-planning strategy is contemplated, and management determines this strategy would more likely than not enable the reporting entity to realize the full or a partial amount of its adjusted gross deferred tax assets, paragraph 3 of this statement related to tax loss contingencies shall be applied in determining admissibility of deferred tax assets under paragraph 11 of this statement.

Intercompany Income Tax Transactions

16. In the case of a reporting entity that files a consolidated income tax return with one or more affiliates, income tax transactions (including payment of tax contingencies to its parent) between the affiliated parties shall be recognized if:

a. Such transactions are economic transactions as defined in *SSAP No. 25—Affiliates and Other Related Parties* (SSAP No. 25);

b. Are pursuant to a written income tax allocation agreement; and

c. Income taxes incurred are accounted for in a manner consistent with the principles of FAS 109, as modified by this statement.

17. Amounts owed to a reporting entity pursuant to a recognized transaction shall be treated as a loan or advance, and nonadmitted, pursuant to SSAP No. 25, to the extent that the recoverable is not settled within 90 days of the filing of a consolidated income tax return, or where a refund is due the reporting entity's parent, within 90 days of the receipt of such refund.

Intraperiod Tax Allocation

18. In accordance with paragraph 35 of FAS 109, a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL. The amount allocated shall be computed in a manner consistent with paragraph 38 of FAS 109.

19. Income taxes incurred shall be allocated to net income and realized capital gains or losses in a manner consistent with paragraph 38 of FAS 109. Furthermore, income taxes incurred or received during the current year attributable to prior years shall be allocated, to the extent not previously provided, to net

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income in accordance with SSAP No. 3 unless attributable, in whole or in part, to realized capital gains or losses, in which case, such amounts shall be apportioned between net income and realized capital gains and losses, as appropriate.

Interim Periods

20. Income taxes incurred in interim periods shall be computed using an estimated annual effective current tax rate for the annual period in accordance with the methodology described in paragraphs 19 and 20 of *Accounting Principles Board Opinion No. 28, Interim Financial Reporting*. Estimates of the annual effective tax rate at the end of interim periods are, of necessity, based on estimates and are subject to subsequent refinement or revision. If a reliable estimate cannot be made, the actual effective tax rate for the year-to-date may be the best estimate of the annual effective tax rate. If a reporting entity is unable to estimate a part of its "ordinary" income (or loss) or the related tax (or benefit) but is otherwise able to make a reliable estimate, the tax (or benefit) applicable to the item that cannot be estimated shall be reported in the interim period in which the item is reported.

Disclosures

21. Statutory financial statement disclosures shall be made in a manner consistent with the provisions of paragraphs 43-45 and 48 of FAS 109. However, required disclosures with regard to a reporting entity's GAAP valuation allowance shall be replaced with disclosures relating to the statutory valuation allowance adjustment and the nonadmittance of some portion or all of a reporting entity's DTAs. The financial statements shall include the disclosures required by paragraph 47 of FAS 109 for non-public companies. Paragraphs 22-28 describe the disclosure requirements as modified for the difference between the requirements of FAS 109 and those prescribed by this statement.

22. The components of the net DTA or DTL recognized in a reporting entity's financial statements shall be disclosed as follows:

a. The total of all DTAs (gross, adjusted gross, admitted and nonadmitted) by tax character;

b. The total of all DTLs by tax character;

c. The total DTAs nonadmitted as the result of the application of paragraph 11;

d. The net change during the year in the total DTAs nonadmitted;

e. The amount of each result or component of the calculation, by tax character of paragraphs 11.a., 11.b.i., 11.b.ii., and the ExDTA ACL RBC Ratio, the ExDTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital Ratio, or the Adjusted Gross DTA/Adjusted Capital and Surplus Ratio used in the applicable *Realization Threshold Limitation Table* (the RBC Reporting Entity Table, the Financial Guaranty or

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Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) in paragraph 11.b., as applicable; and

f. The impact of tax-planning strategies on the determination of adjusted gross DTAs and the determination of net admitted DTAs, by percentage and by tax character, and whether the tax-planning strategies include the use of reinsurance-related tax planning strategies.

23. To the extent that DTLs are not recognized for amounts described in paragraph 31 of FAS 109, the following shall be disclosed:

a. A description of the types of temporary differences for which a DTL has not been recognized and the types of events that would cause those temporary differences to become taxable;

b. The cumulative amount of each type of temporary difference;

c. The amount of the unrecognized DTL for temporary differences related to investments in foreign subsidiaries and foreign corporate joint ventures that are essentially permanent in duration if determination of that liability is practicable or a statement that determination is not practicable; and

d. The amount of the DTL for temporary differences other than those in paragraph 23.c. that is not recognized in accordance with the provisions of paragraphs 31 of FAS 109.

24. The significant components of income taxes incurred (i.e., current income tax expense) and the changes in DTAs and DTLs shall be disclosed. Those components would include, for example:

a. Current tax expense or benefit;

b. The change in DTAs and DTLs (exclusive of the effects of other components listed below);

c. Investment tax credits;

d. The benefits of operating loss carryforwards;

e. Adjustments of a DTA or DTL for enacted changes in tax laws or rates or a change in the tax status of the reporting entity; and

f. Adjustments to gross deferred tax assets because of a change in circumstances that causes a change in judgment about the realizability of the related deferred tax asset, and the reason for the adjustment and change in judgment.

25. Additionally, to the extent that the sum of a reporting entity's income taxes incurred and the change in its DTAs and DTLs is different from the result obtained by applying the federal statutory rate

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to its pretax net income, a reporting entity shall disclose the nature of the significant reconciling items.

26. A reporting entity shall also disclose the following:

a. The amounts, origination dates and expiration dates of operating loss and tax credit carryforwards available for tax purposes;

b. The amount of federal income taxes incurred in the current year and each preceding year, which are available for recoupment in the event of future net losses; and

c. The aggregate amount of deposits admitted under Section 6603 of the Internal Revenue Service Code.

27. For any federal or foreign income tax loss contingencies as determined in accordance with paragraph 3.a. for which it is reasonably possible that the total liability will significantly increase within 12 months of the reporting date, the reporting entity shall disclose an estimate of the range of the reasonably possible increase or a statement that an estimate of the range cannot be made.

28. If a reporting entity's federal income tax return is consolidated with those of any other entity or entities, the following shall be disclosed:

a. A list of names of the entities with whom the reporting entity's federal income tax return is consolidated for the current year; and

b. The substance of the written agreement, approved by the reporting entity's Board of Directors, which sets forth the manner in which the total combined federal income tax for all entities is allocated to each entity which is a party to the consolidation. (If no written agreement has been executed, give an explanation of why such an agreement has not been executed.) Additionally, the disclosure shall include the manner in which the entity has an enforceable right to recoup federal income taxes in the event of future net losses which it may incur or to recoup its net losses carried forward as an offset to future net income subject to federal income taxes.

29. Refer to the Preamble for further discussion regarding disclosure requirements.

Relevant Literature

30. This statement adopts the provisions of FAS 109 except as modified in paragraph 2 of this statement which results in paragraphs 29-30, 36-37, 39, 41-42, 46, and 49-59 of FAS 109 being rejected, inasmuch as they are not applicable to reporting entities subject to this statement or are inconsistent with other statutory accounting principles. Paragraph 47 of FAS 109 is adopted with modification to provide for the disclosures required for non public reporting entities. This statement rejects *ASU 2016-16, Intra-Entity Transfers of Assets Other than Inventory.*

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31. This statement rejects *ASU 2015-17 Balance Sheet Classification of Deferred Taxes*, *FASB Interpretation No. 18, Accounting for Income Taxes in Interim Periods…an interpretation of APB Opinion No. 28* and *FIN 48: Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109.*

32. The following lists FASB Staff Positions that are adopted or rejected by this statement:

a. *FASB Staff Position FAS 109-1, Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004* is adopted in its entirety.

b. *FASB Staff Position FAS 109-2, Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision within the American Jobs Creation Act of 2004* is rejected in its entirety.

c. *FASB Staff Position FIN 48-2, Effective Date of FIN 48 for Certain Nonpublic Enterprises* is rejected in its entirety.

d. *FASB Staff Position FIN 48-3, Effective Date of FIN 48 for Certain Nonpublic Enterprises* is rejected in its entirety.

33. The following lists Accounting Principles Board Opinions that are adopted or rejected by this statement:

a. *Accounting Principles Board Opinion No. 2, Accounting for the "Investment Credit,"* paragraphs 9-15 are adopted with modification to utilize the cost reduction method only and rejects all other paragraphs;

b. *Accounting Principles Board Opinion No. 4 (Amending No. 2), Accounting for the "Investment Credit,"* is rejected in its entirety;

c. *Accounting Principles Board Opinion No. 10, Omnibus Opinion—1966,* paragraph 6 is adopted;

d. *Accounting Principles Board Opinion No. 23, Accounting for Income Taxes—Special Areas,* paragraphs 1-3, 5-9, 12-13, and 15-18 are adopted, and paragraphs 19-25, and 31-33 are rejected;

e. *Accounting Principles Board Opinion No. 28, Interim Financial Reporting,* paragraphs 19 and 20 are adopted and all other paragraphs rejected.

34. The following lists FASB Technical Bulletins that are adopted or rejected by this statement:

a. *FASB Technical Bulletin No. 79-9, Accounting in Interim Periods for Changes in Income Tax Rates* is rejected in its entirety;

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b. *FASB Technical Bulletin No. 82-1, Disclosure of the Sale or Purchase of Tax Benefits through Tax Leases* is adopted in its entirety.

35. The following lists FASB Emerging Issues Task Force Issues that are adopted or rejected by this statement:

a. *FASB Emerging Issues Task Force No. 91-8, Application of FASB Statement No. 96 to a State Tax Based on the Greater of a Franchise Tax or an Income Tax,* is rejected in its entirety;

b. *FASB Emerging Issues Task Force No. 92-8, Accounting for the Income Tax Effects under FASB Statement No. 109 of a Change in Functional Currency When an Economy Ceases to Be Considered Highly Inflationary*, is adopted in its entirety;

c. *FASB Emerging Issues Task Force No. 93-13, Effect of a Retroactive Change in Enacted Tax Rates That Is Included in Income from Continuing Operations*, is rejected in its entirety;

d. *FASB Emerging Issues Task Force No. 93-16, Application of FASB Statement No. 109 to Basis Differences within Foreign Subsidiaries That Meet the Indefinite Reversal Criterion of APB Opinion No. 23*, is rejected in its entirety;

e. *FASB Emerging Issues Task Force No. 93-17, Recognition of Deferred Tax Assets for a Parent Company's Excess Tax Basis in the Stock of a Subsidiary That Is Accounted for as a Discontinued Operation*, is adopted in its entirety;

f. *FASB Emerging Issues Task Force No. 94-10, Accounting by a Company for the Income Tax Effects of Transactions among or with Its Shareholders under FASB Statement No. 109*, is rejected in its entirety;

g. *FASB Emerging Issues Task Force No. 95-9, Accounting for Tax Effects of Dividends in France in Accordance with FASB Statement No. 109*, is rejected in its entirety;

h. *FASB Emerging Issues Task Force No. 95-10, Accounting for Tax Credits Related to Dividend Payments in Accordance with FASB Statement No. 109*, is rejected in its entirety;

i. *FASB Emerging Issues Task Force No. 95-20, Measurement in the Consolidated Financial Statements of a Parent of the Tax Effects Related to the Operations of a Foreign Subsidiary That Receives Tax Credits Related to Dividend Payments*, is rejected in its entirety.

36. This statement rejects *AICPA Accounting Interpretations, Accounting for the Investment Credit: Accounting Interpretations of APB Opinion No. 4* in its entirety.

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Effective Date and Transition

37. This statement shall be effective for years beginning January 1, 2012. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

REFERENCES

Relevant Issue Papers

- *Issue Paper No. 83—Accounting for Income Taxes*

EXHIBIT A – IMPLEMENTATION QUESTIONS AND ANSWERS

The National Association of Insurance Commissioners issued *SSAP No. 101—Income Taxes* (SSAP No. 101) with an effective date of January 1, 2012.

This Q&A is effective for reporting periods ending on or after January 1, 2012.

Index to Questions:

Question No.	Question	SSAP No. 101 Paragraph Reference
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	carryforwards determined for SSAP No. 101 purposes?	and 12.a.
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7	What is the meaning of the term "taxes paid"?	11.a.
8	How is a company's computation of adjusted gross and admitted adjusted gross deferred taxes impacted if it joins in the filing of a consolidated federal income tax return?	7, 11, 12.c. and 16
9a	How does the modification provided in paragraph 3.a.iii. impact the calculation of the tax contingencies recorded?	3.a.iii.
9b	What impact, if any, does the inclusion of tax contingencies as a component of current income taxes have on the determination of deferred income taxes?	3.a. and 3.c.
10a	If the reporting entity adjusts the amount of regular taxable income and capital gains reported on a prior year income tax return from the amount originally determined for financial reporting purposes, how is the effect of the change reported in the current year?	19
10b	What is meant by the phrase in paragraph 18 "a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL"?	18
11	How are current and deferred income taxes to be accounted for in interim periods?	12.d. and 20
12	How do you present deferred taxes in the Annual Statement?	8, 18 and 21-28
13	How are tax-planning strategies to be considered in determining adjusted gross DTAs and admitted adjusted gross DTAs?	11.a., 11.b.i., 14 and 15

1. Q – What are the primary differences between the accounting for income taxes pursuant to FAS 109 and SSAP No. 101? [No specific paragraph reference]

1.1 A – SSAP No. 101 establishes statutory accounting principles for current and deferred federal and foreign income taxes and current state income taxes. In general, SSAP No. 101 adopts the concepts of FAS 109, with modifications. The primary differences and modifications are summarized below:

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1.2 State Income Tax

- FAS 109 – State income taxes should be included as "income taxes incurred." Deferred state income taxes are recognized.

- SSAP No. 101 – State income taxes should be included as "Taxes, Licenses, and Fees" by property and casualty insurers and as "Insurance taxes, licenses, and fees, excluding federal income taxes" by life and accident and health insurers. No deferred state income taxes are recognized.

1.3 Valuation Allowance

- FAS 109 – Gross deferred tax assets (DTAs) are reduced by a valuation allowance if it is more likely than not that some portion or all of the DTAs will not be realized. The valuation allowance should be sufficient to reduce the DTA to the amount that is more likely than not to be realized.

- SSAP No. 101 – Gross DTAs are reduced by a statutory valuation allowance adjustment that is determined on a separate company, reporting entity basis. Pursuant to paragraphs 2 and 7.e. of SSAP No. 101, gross DTAs are adjusted to an amount that is more likely than not to be realized (a likelihood of more than 50 percent). Only adjusted gross DTAs shall be considered in determining admitted adjusted gross DTAs. See Question 2 for further discussion of the statutory valuation allowance adjustment. See Question 4 for a further discussion of the admissibility test. See Question 12 for further discussion of presentation and disclosure of the statutory valuation allowance adjustment.

1.4 Unique Statutory Accounting Items

- FAS 109 – In general, the effects of all temporary differences must be reflected with limited exceptions provided in FAS 109 paragraphs 31-34 (relating to items specified in Accounting Principles Board Opinion No. 23) and for temporary differences related to goodwill for which amortization is not deductible for tax purposes.

- SSAP No. 101 – In addition to the exceptions provided in FAS 109, temporary differences do not include asset valuation reserve (AVR), interest maintenance reserve (IMR), Schedule F penalties and, in the case of a mortgage guaranty insurer, amounts attributable to its statutory contingency reserve to the extent that "tax and loss" bonds have been purchased.

1.5 Changes in Deferred Tax Assets and Liabilities

- FAS 109 – Changes in DTAs and deferred tax liabilities (DTLs) are included in income tax expense or benefit and are allocated to continuing operations, discontinued operations, extraordinary items and items charged directly to shareholders' equity.

- SSAP No. 101 – Changes in DTAs and DTLs are recognized as a separate component of

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gains and losses in surplus, except to the extent allocated to changes in unrealized gains and losses.

1.6 Regulated Enterprises

- FAS 109 – Regulated enterprises that meet the criteria for application of FAS 71, *Accounting for the Effects of Certain Types of Regulation*, are not exempt from the requirements of FAS 109. However, assets are reported on a net-of-tax basis (see paragraphs 29, 57, 58 and 59 of FAS 109).

- SSAP No. 101 – These special paragraphs do not apply pursuant to paragraph 30 of SSAP No. 101.

1.7 Business Combinations

- FAS 109 – Paragraphs 30 and 53-56 of FAS 109 provide certain guidance regarding the treatment of business combinations. In general, a deferred tax asset or liability is recognized for the differences between the assigned values and the tax bases of the assets and liabilities recognized in a purchased business combination. If financial statements for prior years are restated, all purchase business combinations that were consummated in those prior years shall be remeasured in accordance with FAS 109.

- SSAP No. 101 – These special paragraphs do not apply pursuant to paragraph 30 of SSAP No. 101.

1.8 Intraperiod Tax Allocation

- FAS 109 – Income tax expense or benefit is allocated among continuing operations, discontinued operations, extraordinary items, and items charged or credited directly to shareholders' equity pursuant to paragraphs 36 and 37 of FAS 109.

- SSAP No. 101 – These paragraphs of FAS 109 do not apply pursuant to paragraph 30 of SSAP No. 101. Instead, paragraphs 18 and 19 of SSAP No. 101 provide special rules for statutory accounting. See Question 10 for a further discussion of these rules.

1.9 Certain Quasi-Reorganizations

- FAS 109 – Paragraph 39 provides special rules relating to the treatment of deductible temporary differences and carryforwards as of the date of a quasi-reorganization.

- SSAP No. 101 – Paragraph 39 of FAS 109 does not apply pursuant to paragraph 30 of SSAP No. 101.

1.10 Financial Statement Classification of DTAs and DTLs

- FAS 109 – Pursuant to paragraphs 41 and 42 of FAS 109, DTAs and DTLs are to be

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classified separately as either current or noncurrent, depending on the classification of the related asset or liability. Furthermore, current DTAs and DTLs and noncurrent DTAs and DTLs are netted within the classification and with the net amount reported.

- SSAP No. 101 – These paragraphs do not apply to statutory accounting pursuant to paragraph 30 of SSAP No. 101. The net admitted DTA, or the net DTL, should be reported in the statutory financial statements.

1.11 Accounting for Uncertainty in Income Taxes

- FAS 109 – Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 (FIN 48) provides accounting and reporting guidance for uncertain tax positions under GAAP.

- SSAP No. 101 – FIN 48 is rejected for statutory accounting pursuant to paragraph 31 of SSAP No. 101. *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* (SSAP No. 5R) provides guidance in determining the amount of federal and foreign income tax loss contingencies with the following modifications. The term "probable" as used in SSAP No. 5R is replaced by the term "more likely than not (a likelihood of more than 50 percent)". In determining the amount of a federal or foreign income tax loss contingency, it shall be assumed that the reporting entity will be examined by the tax authority that has full knowledge of all relevant information. If the estimated tax loss contingency is greater than 50% of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% of the original tax benefit recognized. See Question 9 for further discussion of income tax loss contingencies.

1.12 Classification of Interest and Penalties

- FAS 109 – FIN 48 allows interest on tax assessments to be reported as either income taxes or interest expense and penalties to be reported as either income taxes or another expense classification, based on the accounting policy election of the enterprise.

- SSAP No. 101 – Interest and penalties related to foreign or federal income tax are included in income taxes pursuant to paragraph 3.a. of SSAP No. 101.

1.13 Financial Statement Disclosures

- FAS 109 – Paragraphs 43-45 and 47-48 of FAS 109 provide various requirements for providing information in the financial statements regarding the income taxes of the reporting entity. In general, the reporting entity is to provide certain information regarding the components of its DTAs and DTLs, the amount of and changes in its valuation allowance, significant components of income tax expense, differences between the expected amount of income tax expense using current tax rates and the amount of reported income tax expense,

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and tax attributes being carried over. In addition, FIN 48 includes specific disclosures related to uncertain tax positions.

- SSAP No. 101 – In general, paragraphs 21-29 of SSAP No. 101 follow the disclosure requirements provided by FAS 109, but with the following modifications and additions:
  - The disclosures regarding valuation allowance are replaced with disclosures relating to the statutory valuation allowance adjustment and the nonadmitted portion of the DTA.
  - The amount of the gross DTA, adjusted gross DTA, DTL, admitted and nonadmitted DTA is required to be separately disclosed, by tax character (ordinary or capital).
  - Disclose the amount of each result or component of the admission calculation, by tax character, for paragraphs 11.a, 11.b.i, 11.b.ii, and 11.c. In addition, disclose the ExDTA Authorized Control Level (ACL) RBC Ratio, the ExDTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital Ratio (see paragraph 11.b.), or the Adjusted Gross DTA/Adjusted Capital and Surplus Ratio used in the applicable Realization Threshold Limitation Table (the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table, or the Other Non-RBC Reporting Entity Table) in paragraph 11.b., as applicable.
  - The impact of tax-planning strategies on the determination of adjusted gross DTAs and the determination of net admitted adjusted gross DTAs, by percentage and by tax character, must be disclosed. In addition, disclose whether tax-planning strategies include the use of reinsurance-related tax planning strategies.
  - FIN 48 and the associated disclosure requirements are rejected for statutory accounting purposes and replaced with the following disclosure. For any federal or foreign income tax loss contingencies for which it is reasonably possible that the total liability will significantly increase within 12 months of the reporting date, a disclosure of an estimate of the range of the reasonably possible increase is required. If determination of a reasonable range of the significant increase is not possible, the reporting entity is to provide a statement that an estimate cannot be made.
  - The disclosures relating to deferred income tax expense or benefit are replaced with certain disclosures relating to the reporting entity's "change in DTAs and DTLs."
  - Only the nature of significant reconciling items between the reported amount and "expected" amount of income tax expense and change in DTAs and DTLs are to be disclosed. This generally follows the disclosure requirements of FAS 109 for nonpublic entities.
  - See Question 12 for a more detailed discussion of the disclosure requirements of SSAP No. 101.

2. Q – How should an entity measure its adjusted gross deferred tax assets and its gross

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deferred tax liabilities? [Paragraph 7]

2.1 A – An enterprise shall record a gross deferred tax liability or asset for all temporary differences and operating loss, capital loss and tax credit carryforwards. Temporary differences include unrealized gains and losses and nonadmitted assets but do not include AVR, IMR, Schedule F penalties and, in the case of a mortgage guaranty insurer, amounts attributable to its statutory contingency reserve to the extent that "tax and loss" bonds have been purchased. In general, temporary differences produce taxable income or result in tax deductions when the related asset is recovered or the related liability is settled. A deferred tax asset or liability represents the increase or decrease in taxes payable or refundable in future years as a result of temporary differences and carryforwards at the end of the current year. Additionally, gross DTAs are reduced by a statutory valuation allowance adjustment if, based on the weight of available evidence, it is more likely than not (a likelihood of more than 50 percent) that some portion or all of the gross DTAs will not be realized. The statutory valuation allowance adjustment, determined in a manner consistent with paragraphs 20-25 of FAS 109, shall reduce gross DTAs to the amount that is more likely than not to be realized (the adjusted gross deferred tax assets).[6(151)] This answer only addresses the recognition of adjusted gross DTAs and gross DTLs and does not address the admissibility of such amounts. See Question 4 for a discussion of the admissibility criteria of SSAP No. 101.

2.2 Paragraph 7 of SSAP No. 101 states that temporary differences are identified and measured using a "balance sheet" approach whereby the statutory balance sheet and the tax basis balance sheet are compared. Operating loss, capital loss and tax credit carryforwards are computed in accordance with the applicable Internal Revenue Code.

2.3 The following illustrates the recognition and measurement of a typical book to tax difference for an insurance company:

Illustration

Assumptions:

1/1/X2 Purchase 100 shares of Darby/Allyn Corp. stock for $25 a share
3/31/X2 Fair Value of Darby/Allyn Corp. stock has increased to $35 a share
3/31/X2 Tax basis reserves are computed and determined to be 80% of the statutory basis reserves

Balance Sheet at 3/31/X2:

	Statutory Basis	**Tax Basis**	**Basis Difference**	**Tax Effect DTA (DTL) (35%)[7(152)]**
Common Stock	$3,500	$2,500	($1,000)[8(153)]	($350)
Reserves	$100,000	$80,000	$20,000[9(154)]	$7,000

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Journal Entries:

1/1/X2	DR	Common stock	$2,500
	CR	Cash	($2,500)
		Acquisition of common stock at $25 per share	

3/31/X2	DR	Common stock	$1,000
	CR	Change in unrealized capital gains and losses	($1,000)
		Adjust carrying value to FV of $35 per share at end of quarter	

3/31/X2	DR	Change in reserves or unpaid losses	$100,000
	CR	Reserves or Unpaid losses	($100,000)
		Recognition of reserves computed on a statutory basis	
3/31/X2	DR	Deferred tax asset	$7,000
	CR	Change in deferred income taxes	($6,650)
	CR	Deferred tax liability	($350)
		Recognition of deferred taxes	

NOTE: Presentation of deferred tax amounts and unrealized gain or losses net of tax is addressed in Question 12.

2.4 As depicted in the Illustration, the deferred tax assets and liabilities are tracked gross in the entity's ledger and not netted until after consideration of the statutory valuation allowance adjustment, if any (see below), and the admissibility of deferred tax assets.

Statutory Valuation Allowance Adjustment

2.5 SSAP No. 101 paragraph 7.e. provides that gross DTAs are reduced by a statutory valuation allowance adjustment if, based on the weight of available evidence, it is more likely than not that some portion or all of the gross DTAs will not be realized. The statutory valuation allowance adjustment is determined on a separate company, reporting entity basis. The determination of whether gross DTAs will be realized is based on the existence of sufficient taxable income of the appropriate character (ordinary income or capital gain) within the carryback, carryover period available under the tax law. Paragraph 13.a. through 13.d. of SSAP No. 101 identifies four sources of taxable income to be considered in evaluating the existence of sufficient taxable income. These sources are identical to those to be considered under FAS 109 paragraph 21. FAS 109 paragraph 20 provides that "all available evidence, both positive and negative, should be considered to determine whether, based on the weight of that

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evidence, a valuation allowance is needed. Information about an enterprise's current financial position and its results of operations for the current and preceding years ordinarily is readily available. That historical information is supplemented by all currently available information about future years. Sometimes, however, historical information may not be available (for example, start-up operations) or it may not be as relevant (for example, if there has been a significant, recent change in circumstances) and special attention is required." A reporting entity is not required to consider all four sources of taxable income in determining the need for a statutory valuation allowance adjustment if one or more sources are alone sufficient to support the conclusion that the entity will realize the tax benefits of its gross deferred tax assets (i.e., a conclusion that no valuation allowance is necessary). However, the reporting entity is required to consider all of the potential sources of taxable income to determine the amount of the adjustment if a conclusion is reached that a statutory valuation allowance adjustment is necessary. Historical and/or currently available information may exist that is also significant and relevant in determining the amount of the DTAs admitted under paragraph 11 of SSAP No. 101. This historical and/or currently available information must also be considered when determining the amount of DTAs admitted under paragraph 11 of SSAP No. 101, irrespective of the conclusion reached in establishing or not establishing a statutory valuation allowance adjustment. See Question 4.13 for specific guidance on the admissibility of DTAs under paragraph 11.c. of SSAP No. 101.

2.6 Footnote 1 to paragraph 7.e. of SSAP No. 101 indicates that a reporting entity shall consider reversal patterns of temporary differences, and might be required to schedule such differences:

> …to the extent necessary to support establishing or not establishing a valuation allowance adjustm determined in accordance with paragraphs 228 and 229 of FAS 109. For purposes of this accour statement, consideration of reversal patterns does not require scheduling beyond that necessar support establishing or not establishing a valuation allowance adjustment.

Paragraph 228 of FAS 109 generally holds that a company may need to schedule its temporary differences to determine the particular years in which the reversal of temporary differences is expected to occur. As discussed in Question 5b, paragraph 229 of FAS 109 indicates that future originating temporary differences and their subsequent reversal should be considered in determining the existence of future taxable income.

2.7 Although a reporting entity may need to consider the reversal pattern of temporary differences in evaluating the need for a statutory valuation allowance adjustment, scheduling the reversal pattern of such differences is not required in every instance. Under SSAP No. 101 and consistent with FAS 109, a general understanding of reversal patterns is, in many cases, relevant in assessing the need for a valuation allowance. Judgment is crucial in making this assessment. The amount of scheduling, if any, that will be required will depend on the facts and circumstances of each situation. For example, a reporting entity which relies upon future taxable income exclusive of reversing temporary differences and carryforwards[10(155)] for realization of DTAs is not required to schedule the reversal pattern of its existing temporary differences. This is consistent with guidance provided by the Financial Accounting Standards Board (FASB) in its answer to question 2 of *A Guide to Implementation of Statement 109 on Accounting for Income Taxes: Question and Answers* (Special Report on Statement 109) which states that scheduling of existing temporary differences is unnecessary for purposes of determining the need for a valuation allowance "where it can be easily demonstrated that future taxable income will more likely than not be

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adequate to realize future tax benefits of existing deferred tax assets." In contrast, a reporting entity which relies upon the future reversal of existing taxable temporary differences to realize the tax benefits of its deductible temporary differences and carryforwards may be required to consider the reversal patterns of its taxable temporary differences.[11(156)] The degree of scheduling required, however, depends on the facts and circumstances of each situation and the relative magnitude of the taxable and deductible temporary differences. In certain situations, the ability to reasonably conclude that reversing taxable temporary differences will more likely than not create sufficient taxable income to realize reversing deductible temporary differences can be done without detailed scheduling.[12(157)]

2.8 If scheduling is considered necessary, the amount of scheduling required will depend on the particular facts and circumstances and be subject to judgment. There may be more than one acceptable approach. The FASB's answer to question 1 of the Special Report on Statement 109 indicates that the following concepts underlie the determination of reversal patterns under Statement 109:

a. The particular years in which temporary differences result in taxable or deductible amounts generally are determined by the timing of the recovery of the related asset or settlement of the related liability' (paragraph 228).

b. The tax law determines whether future reversals of temporary differences will result in taxable and deductible amounts that offset each other in future years' (paragraph 227).

In addition, the FASB noted that "minimizing complexity is an appropriate consideration in selecting a method for determining reversal patterns"[13(158)], but that the methods used must be systematic and logical and should be consistently applied for all similarly categorized temporary differences and from year to year. Furthermore, the same method should be utilized in determining the reversal patterns in every taxing jurisdiction for which the temporary difference exists.

Grouping of Assets and Liabilities for Measurement

2.9 The manner in which an entity groups its assets and liabilities for measurement shall be conducted in a reasonable and consistent manner. For instance, an entity may group its invested assets into Annual Statement classifications (stocks, bonds, preferred stocks, etc.) or other reasonable groupings (lines of business for grouping its reserves). Entities have the option of recognizing the DTA and DTL within each grouping on a net or gross basis. For instance, a portfolio of common stocks will have both unrealized gain and unrealized losses associated with them. The reporting entity may elect to combine the unrealized gains and losses and compute a single DTA or DTL or it may elect to segregate the unrealized gains from the unrealized losses and compute separate DTAs and DTLs. This option might also arise with respect to depreciable assets. Regardless of which method an entity elects, it is crucial that consistency is maintained to and within each grouping from period to period. An entity shall retain internal documentation to support its grouping in addition to the methodologies employed to arrive at such. An entity is permitted to modify its groupings should events or circumstances change from a previous period. Examples include a change in materiality of underlying assets and liabilities, administrative costs associated with detailing groupings increases or changes in the computer systems that allow more specificity. Entities that modify their groupings should be prepared to rationalize these changes. These entities should also disclose that a modification was made and general reason for such in

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the notes to the financial statements.

Measurement of Nonadmitted Assets

2.10 As noted in paragraph 7.b. of SSAP No. 101, temporary differences include nonadmitted assets. The measurement of these types of assets is not addressed in FAS 109 in that the concept of nonadmission is unique to statutory accounting. For assets that are nonadmitted for statutory accounting purposes, DTAs and DTLs should be measured after nonadmission.

Illustration:

	Statutory Before Nonadmit (Info Purpose)	**Statutory After Nonadmit**	**Tax**	**Basis Difference**[14(159)]	**Tax Effect DTA (DTL) (35%)**
Furniture Fixtures and Equipment	$1,000	0	$1,000		
Accumulated Depreciation	200	0	400		
Basis	$800	0	$600	$600	$210

2.11 The effect of this illustration is a reduction of surplus by $590 ($800 decrease for nonadmitted asset and $210 increase for DTA), provided the resulting DTA meets the admissibility test in paragraph 11 of SSAP No. 101.

3. Q – A reporting entity's deferred tax assets and liabilities are computed using "enacted tax rates." What is the meaning of the term "enacted tax rates"*?* [Paragraph 7.c.]

3.1 A – Paragraph 7.c. of SSAP No.101 provides that total DTAs and DTLs are computed using enacted tax rates.

3.2 Consistent with FAS 109, SSAP No. 101 further requires that deferred tax assets and liabilities be measured using the enacted tax rate that is expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be settled or realized. The effects of future changes in tax rates are not anticipated in the measurement of deferred tax assets and liabilities. Deferred tax assets and liabilities are adjusted for changes in tax rates and other changes in the tax law, and the effects of those changes are recognized at the time the change is enacted.

3.3 Tax laws may apply different tax rates to ordinary income and capital gains. In instances where the enacted tax law provides for different rates on income of different character, deferred tax assets and liabilities should be measured by applying the appropriate enacted tax rate based on the type of taxable or deductible amounts expected to be realized from the reversal of existing temporary differences.

3.4 Currently, under U.S. federal tax law, if taxable income (both ordinary and capital gain) exceeds

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a specified amount, all taxable income is taxed at a single flat tax rate, 35%. Unless graduated tax rates are a significant factor, (i.e., unless the company's taxable income frequently falls below the specified amount), the enacted tax rate is 35% for both ordinary income and capital gain. Alternative minimum tax and the effect of special deductions, such as the small life deduction, are ignored, except to the extent necessary to estimate future taxable income and therefore the enacted rate applicable to that level of taxable income is used.

3.5 If graduated tax rates are expected to be a significant factor in the determination of taxes payable or refundable in future years, deferred tax assets and liabilities should be measured using the average tax rate (based on currently enacted graduated rates) that is expected to apply to estimated average annual taxable income in the period in which the deferred tax asset or liability is expected to be settled or realized. For example, assume a property and casualty insurance company consistently has taxable income less than $10 million, but in excess of $1 million. The enacted graduated rate applicable to that level of taxable income is 34%. Therefore, the reporting entity should use 34% for the determination of its taxes payable or refundable.

3.6 As a reference, FAS 109 paragraphs 18 and 236 provide the following:

18. The objective is to measure a deferred tax liability or asset using the enacted tax rate(s) expected to apply to taxable income in the periods in which the deferred tax liability or asset is expected to be settled or realized. Under current U.S. federal tax law, if taxable income exceeds a specified amount, all taxable income is taxed, in substance, at a single flat tax rate. That tax rate shall be used for measurement of a deferred tax liability or asset by enterprises for which graduated tax rates are not a significant factor. Enterprises for which graduated tax rates are a significant factor shall measure a deferred tax liability or asset using the average graduated tax rate applicable to the amount of estimated annual taxable income in the periods in which the deferred tax liability or asset is estimated to be settled or realized (paragraph 236). Other provisions of enacted tax laws should be considered when determining the tax rate to apply to certain types of temporary differences and carryforwards (for example, the tax law may provide for different tax rates on ordinary income and capital gains). If there is a phased-in change in tax rates, determination of the applicable tax rate requires knowledge about when deferred tax liabilities and assets will be settled and realized.

236. The following example illustrates determination of the average graduated tax rate for measurement of deferred tax liabilities and assets by an enterprise for which graduated tax rates ordinarily are a significant factor. At the end of year 3 (the current year), an enterprise has $1,500 of taxable temporary differences and $900 of deductible temporary differences, which are expected to result in net taxable amounts of approximately $200 on the future tax returns for each of years 4-6. Enacted tax rates are 15 percent for the first $500 of taxable income, 25 percent for the next $500, and 40 percent for taxable income over $1,000. This example assumes that there is no income (for example, capital gains) subject to special tax rates.

The deferred tax liability and asset for those reversing taxable and deductible temporary differences in years 4-6 are measured using the average graduated tax rate for the estimated amount of annual taxable income in future years. Thus, the average graduated tax rate will differ depending on the expected level of annual taxable income (including reversing temporary differences) in years 4-6. The average tax rate will be:

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a. 15 percent if the estimated annual level of taxable income in years 4-6 is $500 or less

b. 20 percent if the estimated annual level of taxable income in years 4-6 is $1,000

c. 30 percent if the estimated annual level of taxable income in years 4-6 is $2,000.

Temporary differences usually do not reverse in equal annual amounts as in the example above, and a different average graduated tax rate might apply to reversals in different future years. However, a detailed analysis to determine the net reversals of temporary differences in each future year usually is not warranted. It is not warranted because the other variable (that is, taxable income or losses exclusive of reversing temporary differences in each of those future years) for determination of the average graduated tax rate in each future year is no more than an estimate. For that reason, an aggregate calculation using a single estimated average graduated tax rate based on estimated average annual taxable income in future years is sufficient. Judgment is permitted, however, to deal with unusual situations, for example, an abnormally large temporary difference that will reverse in a single future year, or an abnormal level of taxable income that is expected for a single future year. The lowest graduated tax rate should be used whenever the estimated average graduated tax rate otherwise would be zero.

4a. Q – How should a reporting entity calculate the amount of its admitted adjusted gross DTAs? [Paragraph 11]

4.1 A – After a reporting entity has calculated the amount of its adjusted gross DTAs and gross DTLs pursuant to paragraph 7, it must determine the amount of its adjusted gross DTAs that can be admitted under paragraph 11. The amount of adjusted gross DTAs is not recalculated under paragraph 11; rather, some or all of the adjusted gross DTA may not be currently admitted.

4.2 Paragraphs 11.a., 11.b. and 11.c. require three interdependent calculations or components that when added together equals the amount of the reporting entity's admitted adjusted gross DTAs. Each of the calculations starts with the total of the reporting entity's adjusted gross DTAs, and determines the amount of such adjusted gross DTAs that can be admitted under that part. For example, the consideration of existing temporary differences in the calculation of admitted adjusted gross DTAs under paragraph 11.a., does not prevent the reconsideration of the same temporary differences in the paragraph 11.b.i. calculation. However, to avoid duplication of admitted adjusted gross DTAs when adding the three parts together, the amount of admitted adjusted gross DTAs under paragraph 11.a. must be subtracted from the amount of adjusted gross DTAs in the paragraph 11.b.i. calculation. Similarly, the amount of admitted adjusted gross DTAs under paragraphs 11.a. and 11.b. must be subtracted from the total adjusted gross DTAs in the paragraph 11.c. calculation.

First Component – Admission Based On Previously Paid Taxes [Paragraph 11.a.]

4.3 Under paragraphs 11.a. and 12.b., a reporting entity can admit adjusted gross DTAs to the extent that it would be able to recover federal income taxes paid in the carryback period, by treating existing temporary differences that reverse during a timeframe corresponding with Internal Revenue Code tax loss carryback provisions[15(160)], not to exceed three years as ordinary or capital losses that originated in each such subsequent year. The reversing temporary differences are specific to each year in which they

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reverse, and in turn, to the specific year(s) to which they can be carried back corresponding with tax loss carryback provisions. Reversing temporary differences for unrealized losses and nonadmitted assets are treated as capital or ordinary losses depending on their character for tax purposes. The entity is not required to project an actual net operating loss in future periods. This first component of admission is available to all entities, regardless of whether they meet any of the threshold limitations in paragraph 11.b. for reversals expected to be realized against future taxable income.

4.4 Paragraph 12.b. limits the amount of federal income taxes recoverable under paragraph 11.a. to the amount that would be refunded to the reporting entity if a carryback claim was filed with the Internal Revenue Service (IRS). If some amount of taxes paid in the carryback period is not recovered because of limitations imposed by the Alternative Minimum Tax system, the resulting AMT credit is not treated as a newly created DTA. Paragraph 12.c. further limits the amount of federal income taxes recoverable under paragraph 11.a. for a reporting entity that files a consolidated income tax return with one or more affiliates, to the amount that the reporting entity could reasonably expect to have refunded by its parent. See Question 8 for a further discussion of the impact of filing a consolidated federal income tax return.

Second Component – Admission Based On Projected Future Tax Savings [Paragraph 11.b.]

4.5 The amount of a reporting entity's adjusted gross DTAs that can be admitted pursuant to paragraph 11.b. is in part, dependent on the amount of the reporting entity's adjusted capital and surplus. Accordingly, a reporting entity must determine which Realization Threshold Limitation Table set forth in paragraph 11.b. is applicable to the reporting entity and then, based on its respective facts, determine what applicable period to apply under paragraph 11.b.i. and applicable percentage to use under paragraph 11.b.ii.

4.6 If the reporting entity is subject to risk-based capital requirements or is required to file a Risk-Based Capital Report with the domiciliary state, it should use the RBC Reporting Entity Table set forth in paragraph 11.b. Threshold limitations for this table are contingent upon the ExDTA ACL RBC ratio. See Question 4b for a discussion on the ExDTA ACL RBC ratio.

4.7 If the reporting entity is (1) either a mortgage guaranty insurer or financial guaranty insurer that is not subject to risk-based capital requirements, (2) is not required to file a Risk-Based Capital Report with the domiciliary state, and (3) the reporting entity meets the minimum capital and reserve requirements[16(161)] for the state of domicile, then it should use the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table set forth in paragraph 11.b. Threshold limitations for this table are contingent upon the ratio of ExDTA Surplus plus contingency reserves divided by the minimum aggregate capital required (see further detail in paragraph 11.b.).

4.8 If the reporting entity (1) is not subject to risk-based capital requirements, (2) is not required to file a Risk-Based Capital Report with the domiciliary state, (3) is not a mortgage guaranty or financial guaranty insurer, and (4) meets the minimum capital and reserve requirements[17(162)], it should use the Other Non-RBC Reporting Entity Table set forth in paragraph 11.b. Threshold limitations for this table are contingent upon the ratio of adjusted gross DTA less the amount of adjusted gross DTA admitted in paragraph 11.a. to adjusted capital and surplus.

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4.9 The amount of admitted adjusted gross DTAs under paragraph 11.b.i., is limited to the amount that the reporting entity expects to realize within the applicable period as determined using the applicable *Realization Threshold Limitation Table* following the balance sheet date. See Question 6 for a further discussion of the meaning of "expected to be realized." The amount of admitted adjusted gross DTAs under the paragraph 11.a. calculation is subtracted from the amount of adjusted gross DTAs under paragraph 11.b.i., to prevent the counting of the same admitted adjusted gross DTAs more than once. If the reporting entity expects to realize an amount of adjusted gross DTAs under paragraph 11.b.i. that is equal to or less than the admitted adjusted gross DTAs calculated under paragraph 11.a., then the resulting admitted adjusted gross DTAs under paragraph 11.b.i. will be zero.

4.10 The reference to applicable period following the balance sheet date in 4.9 refers to the paragraph 11.b.i. column of the applicable Realization Threshold Limitation Table, the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table or the Other Non-RBC Reporting Entity Table.

4.11 The amount of admitted adjusted gross DTAs under paragraph 11.b.i. is also limited to an amount that is no greater than the applicable percentage of adjusted statutory capital and surplus specified in paragraph 11.b.ii. See Question 4c for a discussion of the meaning of "an amount that is no greater than".

4.12 The reference to an amount no greater than the applicable percentage of statutory capital and surplus in 4.11 refers to the 11.b.ii. column of the applicable Realization Threshold Limitation Table; the RBC Reporting Entity Table, the Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Table or the Other Non-RBC Reporting Entity Table.

Third Component – Admission Based On Offset Against DTL [Paragraph 11.c.]

4.13 Under paragraph 11.c., a reporting entity can admit adjusted gross DTAs as an offset against gross DTLs in an amount equal to the lesser of: (1) its adjusted gross DTAs, after subtracting the amount of admitted adjusted gross DTAs under paragraphs 11.a. and 11.b., or (2) its gross DTLs. In determining the amount of adjusted gross DTAs that can be offset against existing gross DTLs in the paragraph 11.c. calculation, the character (i.e., ordinary versus capital) of the DTAs and DTLs must be taken into consideration such that offsetting would be permitted in the tax return under existing enacted federal income tax laws and regulations. For example, an adjusted gross DTA related to unrealized capital losses could not be offset against an ordinary income DTL. Ordinary DTAs can be admitted by offset with ordinary DTLs and/or capital DTLs. However, capital DTAs can only be admitted by offset with capital DTLs. In addition to consideration of the character of the DTAs and DTLs, significant and relevant historical and/or currently available information may exist specific to the remaining adjusted gross DTAs and gross DTLs. This information must also be taken into consideration when determining admission by offset with gross DTLs. As stated in paragraph 11.c., "for purposes of this component, the reporting entity shall consider the reversal patterns of temporary differences; however, this consideration does not require scheduling beyond that required in paragraph 7.e." This consideration requires a scheduling exercise if scheduling is needed for determination of the statutory valuation allowance adjustment and, as a result, should be consistent with the determination of any statutory valuation allowance adjustment, which occurs prior to performing the admissibility calculations.[18(163)] As noted in Question 2.7,

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scheduling reversal patterns of temporary differences in evaluating the need for a statutory valuation allowance adjustment where a reporting entity relies on sources of future taxable income, exclusive of reversals of temporary differences, is not required. In such case, that reporting entity is not required to schedule reversal patterns of temporary differences for purposes of paragraph 11.c. of SSAP No. 101. However, the significant and relevant historical and/or currently available information noted above must be considered and be consistent with the conclusion to admit or nonadmit adjusted gross DTAs under paragraph 11.c. without additional detailed scheduling. See Question 2.5 through 2.8 for further discussion of scheduling for purposes of determining the reporting entity's statutory valuation allowance adjustment.

Other Considerations

4.14 In certain situations, a reporting entity's expected federal income tax rate on its reversing temporary differences will be less than the enacted tax rate used in the determination of its gross DTAs and DTLs. Examples of such entities include: property/casualty insurance companies with large municipal bond portfolios that are AMT taxpayers, Blue Cross-Blue Shield Organizations with section 833(b) deductions, small life insurance companies, reporting entities projecting a tax loss, and entities that file in a consolidated federal income tax return that cannot realize the full amount of their adjusted gross DTAs under the existing intercompany tax sharing or tax allocation agreement. Pursuant to paragraphs 231, 232 and 238 of FAS 109, such entities are required to report their gross DTLs at the enacted tax rate, and cannot take into consideration the impact of the AMT, section 833(b) deduction, or the small life insurance company deduction to reduce their gross DTLs.

4.15 For those entities, the amount of admitted adjusted gross DTAs calculated under paragraphs 11.a. and 11.b. will reflect the actual tax rate in the carryback period under paragraph 11.a. and the expected tax rate in the applicable period as discussed in 4.10 above under paragraph 11.b., which takes into consideration the impact of the AMT, special deductions, and the provisions of the intercompany tax sharing or allocation agreement. See Question 6 for further discussion of this issue. As such, the entity's admitted adjusted gross DTAs under paragraphs 11.a. and 11.b. may be less than its adjusted gross DTAs on temporary differences at the enacted rate. Any unused amount of DTAs resulting from a rate differential under paragraphs 11.a. and 11.b. can be used under paragraph 11.c. to offset existing DTLs.

4.16 The above principles can be illustrated by the following examples:

4.17 Facts:

RBC Reporting Entity Example

1. Life Insurance Company ABC[19(164)] has $12,500,000 of deductible temporary differences at 12-31-20X2 that generate $4,375,000 of gross DTAs ($2,100,000 Ordinary, $2,275,000 Capital), at the enacted federal income tax rate of 35%. Management has concluded that ABC will more likely than not realize gross DTAs of $4,100,000 ($2,100,000 Ordinary, $2,000,000 Capital) related to its $12.5 million of deductible temporary differences. Based on management's conclusion, a statutory valuation allowance adjustment was recognized for $275,000 reducing capital DTAs from $2,275,000 to $2,000,000. ABC also has $4,000,000 of

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taxable temporary differences resulting in $1,400,000 ($1,000,000 Ordinary, $400,000 Capital) of gross DTLs.

2. ABC has determined that $2,000,000 of its $6,000,000 existing deductible ordinary temporary differences will reverse in 12-31-20X3, another $1,500,000 will reverse in 12-31-20X4, and another $2,000,000 will reverse in 12-31-20X5. The remaining $500,000 of ABC's existing deductible ordinary temporary differences will reverse in years 20X6 or later. None of ABC's deductible capital temporary differences are expected to reverse within the applicable period.

3. ABC reported $400,000 and $600,000 of taxable income in 20X0 and 20X1, respectively. ABC reported $140,000 and $210,000 of tax expense on its 20X0 and 20X1 federal income tax returns, respectively. It has also projected taxable income of $1,200,000 and $420,000 of federal income taxes for 20X2 that have been reflected in its current statutory income tax provision calculation. There are no differences between its regular and alternative minimum taxable income during 20X0 through 20X2.

4. ABC is projecting an income tax rate of 35% in 20X3, as well as in years 20X4 and 20X5 based on its estimated taxable income and federal income tax liability. ABC expects to realize[20(165)] a federal income tax benefit of 35% from 20X3 through 20X5 related to reversing ordinary temporary differences. ABC does not anticipate any capital gain income in 20X3 through 20X5.

5. ABC has an ExDTA ACL RBC Ratio at 12-31-20X2 of 600%. Adjusted statutory capital and surplus under paragraph 11.b.ii. is $7,000,000 at 12-31-20X2, and was computed by subtracting the admitted balances of net DTA's, goodwill and EDP from the current period statutory surplus. Statutory surplus is defined in paragraph 2 of SSAP No. 72.

4.18 Calculation of ABC's Admitted Adjusted Gross DTAs:

1. ABC can admit $726,000 ($132,000 + $198,000 + $396,000) of adjusted gross DTAs under paragraph 11.a., all of which are ordinary in tax character.

a. ABC first carries $400,000 of the hypothetical net operating loss[21(166)] of $2,000,000 from 20X3 back to 20X0 recovering $132,000 in taxes paid. The difference between the total 20X0 taxes paid at 35% ($140,000) and the amount recoverable ($132,000) through carryback of the $400,000 represents an $8,000 AMT credit generated as a result of the 90% AMT net operating loss[22(167)] limitation. This AMT credit is not treated as a new DTA as of 12-31-20X2. The remaining $1,600,000 of the hypothetical net operating loss ($2,000,000 – $400,000) is available for utilization in years 20X1 and 20X2.

b. ABC would carry an additional $600,000 of the remaining hypothetical net operating loss of $1,600,000 from 20X3 back to 20X1 recovering $198,000 in

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taxes paid.[23(168)] The difference between the total taxes paid at 35% ($210,000) and the amount recoverable ($198,000) through carryback of the $600,000 represents a $12,000 AMT credit generated as a result of the 90% AMT NOL limitation. Again, this AMT credit is not treated as a new DTA as of 12-31-20X2. The remaining $1,000,000 of hypothetical net operating loss ($1,600,000 – $600,000) is available for utilization in 20X2.

c. ABC would carry the remaining $1,000,000 of the hypothetical net operating loss from 20X3 plus an additional $200,000 of the hypothetical net operating loss from 20X4 back to 20X2, recovering $396,000 in taxes projected to be paid.[24(169)] The difference between the total taxes projected to be paid at 35% ($420,000) and the amount recoverable ($396,000) through carryback of the $1,200,000 represents a $24,000 AMT credit generated as a result of the 90% AMT NOL limitation. As noted previously, this AMT credit is not treated as a new DTA as of 12-31-20X2.

The fact that the full $5,500,000 of reversing deductible ordinary temporary differences available for carryback were not used in the paragraph 11.a. calculation does not prevent their inclusion in the paragraph 11.b. and 11.c. calculations.

2. ABC can admit $1,050,000 of adjusted gross DTAs under paragraph 11.b. Since ABC has an ExDTA ACL RBC ratio of 600%, the Realization Threshold Limitation Table provides that the company can use the thresholds of 3 years for projected realization and 15% of adjusted capital and surplus. The company expects to realize a federal income tax benefit of $1,925,000 ($5,500,000 X 35%) in 20X3 through 20X5 related to its reversing deductible temporary differences. The $1,925,000 amount must be reduced by the $726,000 of admitted adjusted gross DTAs under paragraph 11.a. to prevent double counting of the same income tax benefit. As a result, ABC has projected adjusted gross DTAs available for admission under this component of $1,199,000 ($1,925,000 – $726,000), all of which is ordinary in tax character. However, 15% of adjusted capital and surplus is a limiting factor in this example. As such, admission of reversing deductible temporary differences that are projected to be realized during 20X3 through 20X5 is limited to $1,050,000 ($7,000,000 X 15%).

3. ABC can admit $724,000 ($324,000 Ordinary, $400,000 Capital) of adjusted gross DTAs under paragraph 11.c. Even though ABC has $2,324,000 of adjusted gross DTAs available for admission under this component ($4,100,000 – $726,000 – $1,050,000) and only $1,400,000 DTLs, these DTAs are made up of $324,000 Ordinary DTAs ($2,100,000 – $726,000 – $1,050,000) and $2,000,000 of Capital DTAs. Thus, the tax character of the DTAs and DTLs becomes the limiting factor for this component. There is $1,000,000 of Ordinary DTLs available to offset against the $324,000 of Ordinary DTAs. There is $400,000 of Capital DTLs to offset against the $2,000,000 Capital DTAs. While ordinary DTAs can be offset against both ordinary and capital DTLs, the reverse is not allowed in the tax return (see Question 4.13). In this situation, ABC can admit $324,000 and $400,000 of its Ordinary and Capital DTAs,

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respectively.

4.19 Summary of ABC's Admitted Gross DTA Calculation:

Gross DTAs at Enacted Tax Rate		$4,375,000
Less: Statutory Valuation Allowance Adjustment		275,000
Adjusted Gross DTAs at Enacted Tax Rate		4,100,000
Admitted Gross DTAs (paragraph 11.a.)	$ 726,000	
Admitted Gross DTAs (paragraph 11.b.)	1,050,000	
Admitted Gross DTAs (paragraph 11.c.)	724,000	
Total Admitted Adjusted Gross DTAs(sum of 11.a., 11.b., and 11.c.)	2,500,000	(2,500,000)
Nonadmitted Adjusted Gross DTAs		1,600,000
Admitted DTA		2,500,000
Gross DTL		(1,400,000)
Net Admitted DTA/DTL		$1,100,000

4.20 Facts:

Financial Guaranty or Mortgage Guaranty Non-RBC Reporting Entity Example

1. Financial Guaranty Insurance Company DEF has the same facts as Life Insurance Company ABC except:

a. DEF is not a RBC reporting entity and therefore does not calculate a RBC percentage. DEF is a financial guaranty insurer and has an ExDTA Surplus plus Contingency Reserve/Required Aggregate Risk Capital ratio of 105%. This ratio represents the sum of surplus to policyholders (excluding any admitted DTA from 11.a.) plus contingency reserves divided by the minimum aggregate capital required.

b. DEF reported $1,000,000 of taxable income and $350,000 of tax expense on its 20X1 federal income tax return. It has also projected taxable income of $1,200,000 and $420,000 of federal income taxes for 20X2 that have been reflected in its current statutory income tax provision calculation. There are no differences between its regular and alternative minimum taxable income in 20X1 or 20X2.

4.21 Calculation of DEF's Admitted Adjusted Gross DTAs:

1. DEF can admit $726,000 ($330,000 + $396,000) of adjusted gross DTAs under

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paragraph 11.a, all of which are ordinary in tax character.

a. DEF first carries $1,000,000 of the hypothetical net operating loss[25(170)] of $2,000,000 from 20X3 back to 20X1 recovering $330,000 in taxes paid. The difference between the total 20X1 taxes paid at 35% ($350,000) and the amount recoverable ($330,000) through carryback of the $1,000,000 represents a $20,000 AMT credit generated as a result of the 90% AMT net operating loss limitation. This AMT credit is not treated as a new DTA as of 12-31-20X2. The remaining $1,000,000 of the hypothetical net operating loss ($2,000,000 – $1,000,000) is available for utilization in 20X2.

b. DEF would carry the remaining $1,000,000 of the hypothetical net operating loss from 20X3 plus an additional $200,000 of the hypothetical net operating loss from 20X4 back to 20X2 recovering $396,000 in taxes projected to be paid.[26(171)] The difference between the total taxes projected to be paid at 35% ($420,000) and the amount recoverable ($396,000) through carryback of the $1,200,000 represents a $24,000 AMT credit generated as a result of the 90% AMT net operating loss limitation. As noted previously, this AMT credit is not treated as a new DTA as of 12-31-20X2.

The fact that the full $3,500,000 of reversing deductible ordinary temporary differences available for carryback were not used in the paragraph 11.a. calculation does not prevent their inclusion in the paragraph 11.b. and 11.c. calculations.

2. DEF cannot admit any additional adjusted gross DTAs under paragraph 11.b. Since DEF has an ExDTA Surplus plus Contingency Reserves/Required Aggregate Risk Capital ratio of 105%, the Realization Threshold Limitation Table provides that the company can use the thresholds of 1 year for projected realization and 10% of adjusted capital and surplus. The company expects to realize a federal income tax benefit of $700,000 ($2,000,000 X 35%) in 20X3 related to its reversing deductible temporary differences. The $700,000 amount must be reduced by the $726,000 of admitted adjusted gross DTAs under paragraph 11.a. to prevent double counting of the same income tax benefit. DEF admitted $26,000 more adjusted gross DTAs based on carryback of the hypothetical net operating loss under paragraph 11.a. than is projected to be realized within the 1-year applicable threshold limitation. As a result, there is $0 of expected additional reversing deductible differences available for admission under paragraph 11.b.

3. DEF can admit $1,400,000 ($1,000,000 Ordinary, $400,000 Capital) of adjusted gross DTAs under paragraph 11.c. Even though DEF has $3,374,000 of adjusted gross DTAs available for admission under this component ($4,100,000 – $726,000), these DTAs are made up of $1,374,000 Ordinary DTAs ($2,000,000 – $726,000) and $2,000,000 of Capital DTAs. Thus, the tax character of the DTAs and DTLs must be considered as a potential limiting factor for this component. There is $1,000,000 of Ordinary DTLs to offset against the $1,374,000 of Ordinary DTAs. There is $400,000 of Capital DTLs to offset against the $2,000,000 Capital DTAs. While

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Ordinary DTAs can be offset against both Ordinary and Capital DTLs, the reverse is not allowed in the tax return (see Question 4.13). In this situation, DEF can admit $1,000,000 and $400,000 of its Ordinary and Capital DTAs, respectively. If DEF's adjusted gross DTAs, after reduction for the amount of adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., were less than $1,400,000 in this example, DEF would be limited to the balance of its adjusted gross DTAs in the paragraph 11.c. calculation, subject to the rules of offset under existing enacted federal income tax laws and regulations.

4.22 Summary of DEF's Admitted Gross DTA Calculation:

Gross DTAs at Enacted Tax Rate		$4,375,000
Less: Statutory Valuation Allowance Adjustment		275,000
Adjusted Gross DTAs at Enacted Tax Rate		4,100,000
Admitted Gross DTAs (paragraph 11.a.)	$ 726,000	
Admitted Gross DTAs (paragraph 11.b.)	0	
Admitted Gross DTAs (paragraph 11.c.)	1,400,000	
Total Admitted Adjusted Gross DTAs (sum of 11.a., 11.b. and 11.c.)	2,126,000	(2,126,000)
Nonadmitted Adjusted Gross DTAs		1,974,000
Admitted DTA		2,126,000
Gross DTL		(1,400,000)
Net Admitted DTA/DTL		$726,000

4.23 Facts:

Other Non-RBC Reporting Entity Example

1. Title Insurance Company GHI has the same facts as Life Insurance Company ABC except:

a. GHI is not a RBC reporting entity and therefore does not calculate a RBC percentage. GHI is also not a financial guaranty or mortgage guaranty insurer. As such, GHI must use the Other Non-RBC Reporting Entity Threshold Limitation Table under paragraph 11.b.

b. GHI reported $1,000,000 of taxable income and $350,000 of tax expense on its 20X1 federal income tax return. It has also projected taxable income of $1,200,000 and $420,000 of federal income taxes for 20X2 that have been reflected in its current statutory income tax provision calculation. There are no differences between its regular and alternative minimum taxable income in 20X1 or 20X2.

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4.24 Calculation of GHI's Admitted Adjusted Gross DTAs:

1. GHI can admit $726,000 ($330,000 + $396,000) of adjusted gross DTAs under paragraph 11.a, all of which are ordinary in tax character.

a. GHI first carries $1,000,000 of the hypothetical net operating loss[27(172)] of $2,000,000 from 20X3 back to 20X1 recovering $330,000 in taxes paid. The difference between the total 20X1 taxes paid at 35% ($350,000) and the amount recoverable ($330,000) through carryback of the $1,000,000 represents a $20,000 AMT credit generated as a result of the 90% AMT net operating loss limitation. This AMT credit is not treated as a new DTA as of 12-31-20X2. The remaining $1,000,000 of the hypothetical net operating loss ($2,000,000 – $1,000,000) is available for utilization in 20X2.

b. GHI would carry the remaining $1,000,000 of the hypothetical net operating loss from 20X3 plus an additional $200,000 of the hypothetical net operating loss from 20X4 back to 20X2 recovering $396,000 in taxes projected to be paid.[28(173)] The difference between the total taxes projected to be paid at 35% ($420,000) and the amount recoverable ($396,000) through carryback of the $1,200,000 represents a $24,000 AMT credit generated as a result of the 90% AMT net operating loss limitation. As noted previously, this AMT credit is not treated as a new DTA as of 12-31-20X2.

The fact that the full $3,500,000 of reversing deductible ordinary temporary differences available for carryback were not used in the paragraph 11.a. calculation does not prevent their inclusion in the paragraph 11.b. and 11.c. calculations.

2. GHI can admit $1,050,000 of adjusted gross DTAs under paragraph 11.b. Since GHI has an Adjusted Gross DTA to Adjusted Capital and Surplus ratio of 48% ($3,374,000/$7,000,000), the Realization Threshold Limitation Table provides that the company can use the thresholds of 3 years for projected realization and 15% of adjusted capital and surplus. The company expects to realize a federal income tax benefit of $1,925,000 ($5,500,000 X 35%) in 20X3 through 20X5 related to its reversing deductible temporary differences. The $1,925,000 amount must be reduced by the $726,000 of admitted adjusted gross DTAs under paragraph 11.a. to prevent double counting of the same income tax benefit. As a result, GHI has projected adjusted gross DTAs available for admission under this component of $1,199,000 ($1,925,000 – $726,000), all of which is ordinary in tax character. However, 15% of adjusted capital and surplus is a limiting factor in this example. As such, admission of reversing deductible temporary differences that are projected to be realized during 20X3 through 20X5 is limited to $1,050,000 ($7,000,000 X 15%).

3. GHI can admit $724,000 ($324,000 Ordinary, $400,000 Capital) of adjusted gross DTAs under paragraph 11.c. Even though GHI has $2,324,000 of adjusted gross DTAs available for admission under this component ($4,100,000 – $726,000 – $1,050,000), these DTAs are made up of $324,000 Ordinary DTAs ($2,000,000 – $726,000 – $1,050,000) and $2,000,000 of Capital

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DTAs. Thus, the tax character of the DTAs and DTLs becomes the limiting factor for this component. There is $1,000,000 of Ordinary DTLs available to offset against the $324,000 of Ordinary DTAs. There is $400,000 of Capital DTLs to offset against the $2,000,000 Capital DTAs. While ordinary DTAs can be offset against both ordinary and capital DTLs, the reverse is not allowed in the tax return (see Question 4.13). In this situation, GHI can admit $324,000 and $400,000 of its Ordinary and Capital DTAs, respectively.

4.25 Summary of GHI's Admitted Gross DTA Calculation:

Gross DTAs at Enacted Tax Rate		$4,375,000
Less: Statutory Valuation Allowance Adjustment		275,000
Adjusted Gross DTAs at Enacted Tax Rate		4,100,000
Admitted Gross DTAs (paragraph 11.a.)	$ 726,000	
Admitted Gross DTAs (paragraph 11.b.)	1,050,000	
Admitted Gross DTAs (paragraph 11.c.)	724,000	
Total Admitted Adjusted Gross DTAs (sum of 11.a., 11.b. and 11.c.)	2,500,000	(2,500,000)
Nonadmitted Adjusted Gross DTAs		1,600,000
Admitted DTA		2,500,000
Gross DTL		(1,400,000)
Net Admitted DTA/DTL		$1,100,000

4b. Q – How is the ExDTA ACL RBC ratio calculated? [Paragraph 11.b.i.]

4.26 A – The December 31 ExDTA ACL RBC ratio is calculated in the same manner as in the ACL RBC Ratio computed in the Annual RBC Report, where Total Adjusted Capital (TAC) is divided by ACL RBC. However, for purposes of paragraph 11.b.i., TAC does not include any DTAs of the reporting entity. The ACL RBC would be the amount calculated in the Annual RBC Report.

4.27 The interim period (March 31, June 30, and September 30) ExDTA ACL RBC ratio calculation is discussed in 4.29-4.33.

4.28 For all companies, the TAC will include current period capital and surplus, excluding any DTAs of the reporting entity. Other TAC adjustments are dependent on whether the company is a Life, P&C or Health insurer.

4.29 For life companies, the AVR adjustment is calculated as a required part of the development of capital and surplus each quarter, and is one of the major adjustments to TAC (added back to surplus). As noted on the illustrative interim TAC calculation in 4.33 for life companies, there are other TAC adjustments such as subsidiaries' dividend liabilities, etc., that are drawn from the Quarterly Statement.

4.30 For P&C and Health companies, except for the AVR and life subsidiaries' dividend liability

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amounts (both of which are only applicable to P&C companies with life subsidiaries), which are readily available on the quarter, the prior year's annual TAC adjustments should be used in the current quarter's TAC calculation. The P&C and Health interim TAC illustrations in 4.33 provide example details of various interim RBC TAC adjustments.

4.31 The ACL RBC used for the interim RBC calculation is the ACL RBC from the most recently filed Annual Statement for the most recent calendar year. For example, for June 30, 20X3, the ACL for the interim RBC calculation is taken from the 20X2 RBC Report based on the 20X2 Annual Statement.

4.32 In most instances, the prior year's annual ACL RBC will suffice. A company should only revise its interim ACL RBC for a material change in its risk profile when requested to do so by its domiciliary state or subject to domiciliary state approval.

4.33 The above principles are illustrated below:

Interim Life RBC Example					
Based on the 2011 Life RBC Report page LR033					
		Reported		Interim Period	
	SOURCE OF THE DATA	12/31/20X2		3/31/20X3	
Capital and Surplus	P3, Ln38	$1,800,000,000		$1,700,000,000	
Adjustments:					
AVR	P3, L24.01	60,000,000		65,000,000	
Dividend Liability	P3, L6.1, L6.2 in part	0		0	
Sub AVR	P3, L24.01 of subs	5,000,000		4,500,000	
Sub Dividend Liability	P3, L6.1, L6.2 in part of subs	0		0	
P&C Non-Tabular Discounts and/or Alien Insurance Subsidiary: Other	P&C Subs P3, L1 & L3 in part	0		0	
Hedging Fair Value Adjustment	Company Records	0		0	
Credit for Capital Notes	P3, L24.11	0		0	
Total Adjusted Capital (TAC)	5-Year Historical Data	1,865,000,000		1,769,500,000	
Less: Deferred Tax Asset	P2, C3, L18.2	190,000,000		200,000,000	
TAC ExDTA		$1,675,000,000		$1,569,500,000	
Authorized Control Level RBC	5-Year Historical Data	$175,000,000		$175,000,000	*

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Total Adjusted Capital ExDTA/Authorized Control Level Risk-Based Capital	957%		897%	
* ACL RBC amount for interim period is the 12/31/20X2 amount				

Interim P&C RBC Example				
(Based on the 2011 P&C RBC Report page PR026				
		Reported		Interim Peri
	SOURCE OF THE DATA	12/31/20X2		3/31/20X:
Capital and Surplus	P3, C1, L37 (Ann. & Qtrly. Stmt.)	$850,000,00 0		$765,000.
Adjustments:				
Non-Tabular Discount-Losses	SCHEDULE P P1-SUM C32, L12, (Ann. Stmt. Only)	(800,000)		(800,0
Non-Tabular Discount-Expense	SCHEDULE P P1-SUM C33, L12 (Ann. Stmt. Only)	(60,000)		(60,0
Discount on Medical Loss Reserves Reported as Tabular in Schedule P	Company Records	0		
Discount on Medical Expense Reserves Reported as Tabular In Schedule P	Company Records	0		
P&C Subs Non-Tabular Discount-Losses	SCHEDULE P P1-SUM C32, L12 (Ann. Stmt. Only)	0		
P&C Subs Non-Tabular Discount - Expenses	SCHEDULE P P1-SUM C33, L12 (Ann. Stmt. Only)	0		
P&C Subs Discount on Medical Loss Reserves Reported as Tabular in Schedule P	Subs' Company Records	0		
P&C Subs Discount on Medical Expense Reserves Reported as Tabular In	Subs' Company Records			

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Schedule P		0		
AVR - Life Subs	Subs P3, C1, L24.01 (Ann. & Qtrly. Stmt.)	5,000,000		6,000,
Dividend Liability - Life Subs	Subs P3, C1, L6.1 + l6.2 (Ann. & Qtrly. Stmt.)	0		
Total Adjusted Capital	5-Year Historical Data P17, C1, L28	854,140,000		770,140,
	(Annual/Current calc. on Qtr.)			
Less: Deferred Tax Asset	P2, C3, L18.2 (Ann. & Qtrly. Stmt.)	82,000,000		72,000,
Total Adjusted Capital ExDTA	PR026 (Annual RBC Report/Current Calc. on Qtr.)	772,140,000		698,140,
Authorized Control Level Risk-Based Capital	5-Year Historical Data P17, C1, L29 (Annual)	171,000,000		171,000,
Total Adjusted Capital ExDTA/ Authorized Control Level Risk-Based Capital		452%		4(
* ACL RBC amount for interim period is the 12/31/20X2 amount				

Interim Health RBC Example				
(Based on the 2011 Health RBC Report page XR024				
		Reported		Interim Peri
	SOURCE OF THE DATA	12/31/20X2		3/31/20X3
Capital and Surplus	P3, C3, L33 (Ann. & Qtrly. Stmt.)	$850,000,00 0		$765,000,
Adjustments:				
AVR – Life Subs	Subs' Company Records	0		
Dividend Liability – Life Subs	Subs' Company Records	0		
Tabular Discounts – P&C subs	Subs' Company Records	0		

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Non-Tabular Discounts – P&C Subs	Subs' Company Records	0		
Total Adjusted Capital	5-Year Historical Data P28, C1, L14 (Annual/ Current calc. on Qtr.)	850,000,000		765,000,
Less: Deferred Tax Asset	P2, C3, L18.2 (Ann. & Qtrly. Stmt.)	82,000,000		72,000,
Total Adjusted Capital ExDTA	XR 24 (Annual RBC Report/Current Calc. on Qtr.)	768,000,000		693,000,
Authorized Control Level Risk-Based Capital	5-Year Historical Data P28, C1, L15 (Annual)	171,000,000		171,000,
Total Adjusted Capital ExDTA/ Authorized Control Level Risk-Based Capital		449%		4(
* ACL RBC amount for interim period is the 12/31/20X2 amount				

4c. Q – What is meant by the phrase "an amount that is no greater than"? [Paragraph 11.b.ii.]

4.34 A – As discussed in 4.11 the amount of admitted adjusted gross DTAs under paragraph 11.b.i. is also limited to an amount that is no greater than the applicable percentage of statutory capital and surplus test specified in paragraph 11.b.ii. For purposes of this test, statutory capital and surplus as shown on the statutory balance sheet of the reporting entity for the current period's statement filed with the domiciliary state commissioner is adjusted to exclude any net DTAs, EDP equipment and operating system software and any net positive goodwill.

4.35 The phrase "an amount that is no greater than" in paragraph 11.b.ii. allows an entity to utilize an amount lower (e.g., from the reporting entity's most recently filed statement) than what would be allowed if it utilized the amount of statutory capital and surplus adjusted to exclude any net DTAs, EDP equipment and operating system software and any net positive goodwill as required to be shown on the statutory balance sheet of the reporting entity for the current period's statement filed with the domiciliary state commissioner. This ability to utilize a lower amount is for administrative ease if a reporting entity's surplus is increasing.

4.36 For example, at 12/31/20X2 if adjusted capital and surplus is $100M and at 9/30/20X2 it was $80M, the entity may utilize the $80M amount from the prior quarter.

4.37 If instead 12/31/20X2 adjusted capital and surplus were $60M, the entity may not utilize the

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$80M amount from the prior quarter as that would overstate the limitation under paragraph 11.b.ii.

4.38 If at 12/31/20X2 an entity's adjusted capital and surplus was initially determined to be $150M, the entity can still utilize that amount under paragraph 11.b.ii., if there is a late accounting adjustment that increases that amount to $160M.

5a. Q – How is the timing of reversals of temporary differences and carryforwards determined for SSAP No. 101 purposes? [Paragraphs 7, 11.a., 11.b.i. and 12.a.]

5.1 A – The timing of temporary difference reversals is critical in determining the amount of admitted adjusted gross DTAs. Determining the reversal of temporary differences impacts the adjusted gross DTA admitted pursuant to paragraphs 11.a., 11.b.i. and potentially 11.c. of SSAP No. 101.

5.2 Paragraph 12.a. of SSAP No. 101 states that "For purposes of paragraph 11.a., existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, shall be determined in accordance with paragraphs 228 and 229 of FAS 109." The timing of reversals of temporary differences and carryforwards for purposes of paragraph 11.b. of SSAP No. 101 shall be determined under similar principles.

5.3 Paragraph 228 of FAS 109 states, in pertinent part, that "[t]he particular years in which temporary differences result in taxable or deductible amounts generally are determined by the timing of the recovery of the related asset or settlement of the related liability." Question 1 of the FASB's Special Report on Statement 109 provides additional guidance on scheduling. It defines "scheduling" as the analysis performed to determine the pattern and timing of the reversal of temporary differences. It also provides certain guidelines to be followed, including the need for the method employed to be systematic and logical, that a consistent method be used for each category of temporary differences, and that a change in the method used be considered a change in accounting principle.

5.4 Assume Company A purchases its only asset for $1,000, an asset that is admissible for statutory accounting purposes and depreciated over five years on a straight-line basis. Assume also that the asset is depreciated over seven years for tax purposes using the Modified Accelerated Cost Recovery System (MACRS). The following table summarizes the statutory and tax basis of the asset at the end of each year.

Year	Cost	Statutory Depreciation	Statutory Basis	Tax Depreciation	Tax Basis	Deductible/ (Taxable) Temporary Difference
1	$1,000	$200	$800	$143	$857	$57
2	-	200	600	245	612	12
3	-	200	400	175	437	37
4	-	200	200	125	312	112
5	-	200	-	89	223	223

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6	-	-	-	89	134	134
7	-	-	-	89	45	45
8	-	-	-	45[29](174)	-	-

5.5 At the end of year one, the Company would conclude that $45 ($57 - $12) of the $57 outstanding deductible temporary difference would reverse within one year, leaving a temporary difference of $12 at the end of year two. However, for computing a two or three year reversal, the Company would not project a reversal of the temporary difference by the end of year three or four as the deductible temporary difference is scheduled to increase (from $12 to $37 and from $37 to $112, respectively). If the Company had decided to sell the asset in year two, it may be appropriate to conclude that the outstanding deductible temporary difference of $57 would reverse in year two.

5.6 A similar rationale would apply in the instance of a nonadmitted asset. Assume the same facts as aforementioned, except that the asset is nonadmitted for statutory accounting purposes. The results are summarized in tabular form below.

Year	Cost	Statutory Charge to Surplus	Statutory Basis	Tax Depreciation	Tax Basis	Deductible/ (Taxable) Temporary Difference
1	$1,000	$1,000	-	$143	$857	$857
2	-	-	-	245	612	612
3	-	-	-	175	437	437
4	-	-	-	125	312	312
5	-	-	-	89	223	223
6	-	-	-	89	134	134
7	-	-	-	89	45	45
8	-	-	-	45	-	-

5.7 In this example, the Company has a steady decline in the deductible temporary difference that is not complicated by competing depreciation regimes. This is due to the fact that the Company took the large surplus charge when the asset was nonadmitted, thereby creating a significant deductible temporary difference. The Company would project a $245 temporary difference reversal in year two (from $857 to $612), a $175 temporary difference reversal in year three (from $612 to $437), and a $125 temporary difference reversal in year four (from $437 to $312). Although the Company will take income statement charges for depreciation on the nonadmitted asset, the statutory basis is nonetheless zero from the moment the asset was nonadmitted. Future statutory depreciation deductions will not impact the statutory basis and have no impact on the analysis.

5.8 The above examples assume a single asset. However, the analysis becomes more complicated when the Company has hundreds or thousands of assets within its fixed asset pool. In this instance, it is

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expected that management will make its best estimate of the expected reversal pattern determined in a manner consistent with the grouping for measurement (see question 2 for more discussion about grouping).

5.9 As indicated above, the timing of the reversal of a particular balance sheet item will depend on the expected recovery of the related asset and liability. For example, the temporary difference associated with property & casualty loss reserves would be expected to reverse in a manner consistent with the payout pattern ("development") of the underlying loss reserves. Historical loss development triangles may be useful in substantiating a reversal pattern. For instance, assume Company A writes two types of property and casualty policies: auto liability and workers' compensation. The following table details the components of the statutory and tax reserves for Company A as of December 31, 20X2.

Private Passenger Auto Liability	**Statutory Reserves**	**Tax Reserves**	**Temporary Difference**
AY + 0	$1,000	$900	$100
AY + 1	850	690	160
AY + 2	700	580	120
AY + 3	550	490	60
AY + 4	400	385	15
AY + 5	300	275	25
AY + 6	200	175	25
AY + 7	100	90	10
AY + 8	80	75	5
AY + 9	70	65	5
Prior	50	45	5
Total	$4,300	$3,770	$530

Workers' Compensation	**Statutory Reserves**	**Tax Reserves**	**Temporary Difference**
AY + 0	$1,000	$825	$175
AY + 1	900	800	100
AY + 2	850	770	80
AY + 3	790	695	95
AY + 4	725	610	115
AY + 5	695	600	95
AY + 6	655	575	80
AY + 7	605	545	60

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AY + 8	575	505	70
AY + 9	550	495	55
Prior	505	450	55
Total	$7,850	$6,870	$980

5.10 One option in analyzing the reversal of the temporary difference would be to calculate the historical loss development patterns for the two lines of business by accident year for each year in the applicable reversal period. By applying these development patterns to the individual temporary differences, the Company could estimate the expected reversal of the temporary difference as a whole for each year in the applicable reversal period.

5.11 Another option would be to apply the average development factor by line of business to each reserve for each year in the applicable reversal period. If the average one-year development factor for all accident years for auto liability and workers' compensation were 70% and 35%, respectively, the one-year temporary difference reversal would be $371 ($530 x 70%) for auto liability and $343 ($980 x 35%) for workers' compensation. The same approach could be used in determining the reversal for any other year in the applicable reversal period.

5.12 The temporary difference related to property and casualty unearned premiums is typically twenty percent (20%) of the outstanding statutory unearned premium reserve. If a company issues only one-year policies, it is reasonable to assume that the entire temporary difference will reverse in one year. If a company writes multi-year contracts, management will be required to estimate the percentage of the unearned premium that will be earned within each year of the applicable reversal period and apply these percentages to the outstanding temporary difference.

5.13 The reversal of the temporary difference related to life insurance reserves may require actuarial assistance, normally involving anticipated development of the statutory and tax reserves for policies issued prior to the end of the current reporting year. In computing the anticipated development, it would be expected that reasonable assumptions be used, which may include cash-flow modeling of the entity's reserves. Deferred acquisition costs on life insurance policies are amortized over prescribed periods pursuant to federal tax law. The amortization schedules should provide management with the ability to estimate the reversal for each year in the applicable reversal period with reasonable accuracy.

5.14 For those temporary differences that do not have a defined reversal period, such as unrealized losses on common stock or deferred compensation liabilities, management will need to determine when the temporary difference is "expected" to reverse. For instance, assume a company has an unrealized loss of $200 in its equity portfolio and that, on average, the portfolio turns over twenty-percent (20%) per year. It would be appropriate for the company to conclude that $40 of the temporary difference will reverse in each year in the applicable reversal period. When determining when the temporary difference would be "expected" to reverse, management should normally take into account events that are likely to occur using information, facts and circumstances in existence as of the reporting date. The estimates used in this circumstance should not be extended to other tests of impairment. For instance, when the entity assumed a 20% turnover in its equity portfolio, it is not involuntarily required to record an impairment in

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accordance with paragraph 9 of SSAP No. 30—*Unaffiliated Common Stock*.

5.15 In summary, the methodology used to develop the reversal pattern should be consistent, systematic, and rational. Although consistency is encouraged, business conditions may dictate that certain factors be given more or less weight than in previous periods. Factors to be considered include historical patterns, recent trends, and the likely impact of future initiatives (without regard to future originating temporary differences). For instance, if a company has migrated to a more efficient claims management system, outstanding reserves may be settled more quickly than historical payment patterns may indicate. A company that expects to enter into a loss portfolio transfer reinsurance transaction should consider the implications of that treaty in determining the reversal of the loss reserve temporary difference.

5b. Q – How should future originating differences impact the scheduling of temporary difference reversals during the applicable period? [Paragraphs 11.a., 11.b.i., 11.c. and 12.a]

5.16 A – Future originating differences, and their subsequent reversals, are considered in assessing the existence of future taxable income. However, they should not impact the scheduling of existing temporary difference reversals during the applicable period. Paragraph 229 of FAS 109 provides the following:

> 229. For some assets or liabilities, temporary differences may accumulate over several years and then reverse over several years. That pattern is common for depreciable assets. Future originating differences for existing depreciable assets and their subsequent reversals are a factor to be considered when assessing the likelihood of future taxable income (paragraph 21(b)) for realization of a tax benefit for existing deductible temporary differences and carryforwards.

6. Q – What is meant by the phrase “expected to be realized”? [Paragraph 11.b.i.]

6.1 A – A reporting entity calculates the amount of its adjusted gross DTAs and gross DTLs under paragraph 7 using the enacted tax rate. The amount of adjusted gross DTAs and gross DTLs is not recalculated under paragraph 11. The purpose of paragraph 11 is to determine the amount of adjusted gross DTAs that can be admitted in the reporting period.

6.2 An excerpt of SSAP No. 4 – *Assets and Nonadmitted Assets* indicates:

> 2. For purposes of statutory accounting, an asset shall be defined as: probable[30(175)] future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.

6.3 The phrase “expected to be realized” encompasses a reasonable expectation as to the value of the DTAs consistent with SSAP No. 4. This means that if a reporting entity’s management expects that deductible temporary differences that reverse in the applicable period will produce a federal income tax benefit at a rate that is lower than the enacted rate, the expected rate should be taken into consideration in the determination of the amount of admitted adjusted gross DTAs under paragraph 11.b.i. In other words, available evidence causes the reporting entity to expect the asset to be realized at less than the enacted rate. In such cases, it would not be appropriate to calculate the amount of admitted adjusted gross DTAs

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under paragraph 11.b.i. on the basis of reversing deductible temporary differences at the enacted tax rate.

6.4 The following examples illustrate situations where the amount of admitted adjusted gross DTAs under paragraph 11.b.i. would be less than the adjusted gross DTAs calculated using deductible temporary differences reversing in the applicable period at the enacted income tax rate. The approach in these examples is to determine the tax savings that the company would expect to realize from its reversing deductible temporary differences. This is accomplished through a calculation of the company's income tax liability "with and without" these temporary differences. It is assumed that in these examples there are no prudent and feasible tax-planning strategies that would cause the entity to expect the asset to be realized at a rate different than that presented in the examples.

Example 1:

6.5 P&C has a significant portion of its investment portfolio in municipal bonds. It is estimating regular taxable income to be $6,000,000 in 20X3, $4,000,000 in 20X4, and $5,000,000 in 20X5. Included in these amounts are $10,000,000 ($8,500,000 net of 15% "proration") of excluded tax-exempt interest per year and $2,000,000 of reversing deductible temporary differences per year that were included in P&C's deferred inventory at 12/31/X2. The Company's ExDTA ACL RBC percentage is 700% and therefore required to use the three-year applicable period under paragraph 11.b.i.

20X3	**Without Reversing Temporary Differences**		**With Reversing Temporary Differences**	
	Regular Tax	AMT	Regular Tax	AMT
Regular Taxable Income	$8,000,000	$8,000,000	$8,000,000	$8,000,000
AMT/ACE Adjustment		6,375,000[31(176)]		6,375,000
Reversing Temporary Differences			(2,000,000)	(2,000,000)
Taxable Income	8,000,000	14,375,000	6,000,000	12,375,000
Tax (35% regular/20% AMT)	2,800,000	2,875,000	2,100,000	2,475,000
Tax Liability	$2,800,000	75,000	$2,100,000	375,000
Total Tax		$2,875,000		$2,475,000

20X4	**Without Reversing Temporary Differences**		**With Reversing Temporary Differences**	
	Regular Tax	AMT	Regular Tax	AMT
Regular Taxable Income	$6,000,000	$6,000,000	$6,000,000	$6,000,000
AMT/ACE Adjustment		6,375,000		6,375,000
Reversing Temporary Differences			(2,000,000)	(2,000,000)
Taxable Income	6,000,000	12,375,000	4,000,000	10,375,000
Tax (35% regular/20% AMT)	2,100,000	2,475,000	1,400,000	2,075,000

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Tax Liability	$2,100,000	375,000	$1,400,000	675,000
Total Tax		$2,475,000		$2,075,000

20X5	Without Reversing Temporary Differences		With Reversing Temporary Differences	
	Regular Tax	AMT	Regular Tax	AMT
Regular Taxable Income	$7,000,000	$7,000,000	$7,000,000	$7,000,000
AMT/ACE Adjustment		6,375,000		6,375,000
Reversing Temporary Differences			(2,000,000)	(2,000,000)
Taxable Income	7,000,000	13,375,000	5,000,000	11,375,000
Tax (35% regular/20% AMT)	2,450,000	2,675,000	1,750,000	2,275,000
Tax Liability	$2,450,000	225,000	$1,750,000	525,000
Total Tax		$2,675,000		$2,275,000

Total[32(177)]	Without Reversing Temporary Differences		With Reversing Temporary Differences	
	Regular Tax	AMT	Regular Tax	AMT
Regular Taxable Income	$21,000,000	$21,000,000	$21,000,000	$21,000,000
AMT/ACE Adjustment		19,125,000		19,125,000
Reversing Temporary Differences			(6,000,000)	(6,000,000)
Taxable Income	21,000,000	40,125,000	15,000,000	34,125,000
Tax (35% regular/20% AMT)	7,350,000	8,025,000	5,250,000	6,825,000
Tax Liability	$7,350,000	675,000	$5,250,000	1,575,000
Total Tax		$8,025,000		$6,825,000

6.6 Over the three-year applicable period, the reversing deductible temporary differences of $6,000,000 are expected to save P&C income taxes at a rate of 20% or $1,200,000 ($8,025,000 – $6,825,000). The remaining 15% tax benefit represents an additional AMT credit carryover of $900,000 ($1,575,000 – $675,000). Therefore, P&C's admitted adjusted gross DTAs under paragraph 11.b.i., before reduction for any admitted adjusted gross DTAs under paragraph 11.a. would be $1,200,000, which is less than the amount of its adjusted gross DTAs of $2,100,000 ($6,000,000 x 35%) on reversing deductible temporary differences at the enacted rate. However, the $900,000 difference generated by the 15% (35% - 20%) rate differential under paragraph 11.b.i. would be taken into account in the paragraph 11.c. calculation as part of the amount of adjusted gross DTAs, after application of paragraphs 11.a. and 11.b., that can be offset against existing gross DTLs.

6.7 In the above example, if P&C were to be in a regular tax liability during 20X5 (i.e. a year in the applicable period subsequent to the creation of the 20X3 and 20X4 AMT credit carryovers), these credit

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carryovers may be utilized in determining the 20X5 with and without calculation. This utilization must be within the applicable period and would be limited to the amount allowed under tax law. In Example 1, assuming full utilization of the 20X3 and 20X4 carryovers, in 20X5 the admitted adjusted gross DTAs under paragraph 11.b.i. (before reduction for any admitted adjusted gross DTAs under paragraph 11.a.) would then be equal to the $2,100,000 adjusted gross DTAs on the $6,000,000 of reversing deductible temporary differences because the AMT credit is both generated and fully utilized in the applicable period.

Example 2:

6.8 SL is a small life insurance company with projected assets of less than $500 million at the end of 20X3. SL also estimates that its 20X3 taxable income before the small life insurance company deduction (SLICD) will be $1,300,000. Included in this amount is $400,000 of reversing deductible temporary items that were part of SL's deferred inventory at 12/31/X2. The Company's ExDTA ACL RBC percentage is 250% and therefore it is required to use the one-year applicable period under paragraph 11.b.i.

20X3	**Without Reversing Temporary Differences**		**With Reversing Temporary Differences**	
	Regular Tax	AMT	Regular Tax	AMT
Regular Taxable Income before SLICD	$1,700,000	$1,700,000	$1,700,000	$1,700,000
Reversing Temporary Differences			(400,000)	(400,000)
Net	1,700,000	1,700,000	1,300,000	1,300,000
Small Life Insurance Company Deduction (60%)	(1,020,000)	(1,020,000)	(780,000)	(780,000)
AMT/ACE Adjustment (75% of SLICD)		765,000		585,000
Taxable Income	680,000	1,445,000	520,000	1,105,000
Tax (35% regular/20% AMT)	238,000	289,000	182,000	221,000
Tax Liability	$238,000	51,000	$182,000	39,000
Total Tax		$289,000		$221,000

6.9 Since SL is a small life insurance company with less than $3 million of taxable income before the small life insurance company deduction, it is taxed at an effective federal income tax rate of 17%. The $400,000 of reversing deductible temporary differences in 20X3 is expected to save SL $68,000 ($289,000 - $221,000) in federal income taxes at the 17% rate. The tax savings represents a reduction in regular taxes of $56,000 and AMT taxes of $12,000. Under paragraph 11.b.i., SL would admit adjusted gross DTAs of $68,000, before reduction for any adjusted gross DTAs admitted under paragraph 11.a. Any unused amount of adjusted gross DTAs related to the 18% (35% - 17%) rate differential under paragraph 11.b.i. would be taken into account under paragraph 11.c. as part of the amount of adjusted

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gross DTAs, after reduction for adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., that can be offset against existing gross DTLs. This same approach would be used in 20X4 and 20X5, if the Company instead qualified for the three-year applicable period under paragraph 11.b.i.

Example 3:

6.10 BCBS is a Blue Cross/Blue Shield Organization that expects to fully offset its regular taxable income with available section 833 (b) deductions in 20X2. Prior to considering the section 833 (b) deduction, BCBS projects $8,000,000 of taxable income in 20X3, which includes $3,000,000 of reversing deductible temporary differences that were part of its deferred inventory at 12/31/X2. The Company's ExDTA ACL RBC percentage is 250% and therefore it is required to use the one-year applicable period under paragraph 11.b.i.

6.11 BCBS has a 0% effective tax rate on regular taxable income in 20X3 and is taxed at 20% for AMT. Its regular taxable income is $0, both "with and without" the $3,000,000 reversing deductible temporary differences since the section 833 (b) deduction changes by an equal amount. The $600,000 reduction in AMT tax liability related to the $3,000,000 reversing deduction temporary differences is expected to generate a 20% tax savings in 20X3. Therefore, BCBS would admit $600,000 of adjusted gross DTAs under paragraph 11.b.i., before reduction for any adjusted gross DTAs admitted under paragraph 11.a. Any unused amount of adjusted gross DTAs related to the 15% (35% - 20%) rate differential under paragraph 11.b.i. would be taken into account under paragraph 11.c. as part of the amount of adjusted gross DTAs, after reduction for adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., that can be offset against existing gross DTLs. The same approach would be used in 20X4 and 20X5 if the Company instead qualified for the three-year applicable period under paragraph 11.b.i.

Example 4:

6.12 ABC insurance company is projecting an income tax loss in 20X3 of $20,000,000, which includes $5,000,000 of reversing deductible temporary differences that were part of its deferred inventory at 12/31/X2. ABC expects to pay $0 federal income taxes in 20X3 for both regular and AMT tax purposes as a result of its tax loss. The Company's ExDTA ACL RBC percentage is 250% and therefore, it is required to use the one-year applicable period under paragraph 11.b.i.

20X3	**Without Reversing Temporary Differences**		**With Reversing Temporary Differences**	
	Regular Tax	AMT	Regular Tax	AMT
Regular Taxable Income (Loss)	($15,000,000)	($15,000,000)	($15,000,000)	($15,000,000)
Reversing Temporary Differences			(5,000,000)	(5,000,000)
Taxable Income (Loss)	(15,000,000)	(15,000,000)	(20,000,000)	(20,000,000)
Tax (35% regular/20% AMT)	$0	$0	$0	$0

6.13 In 20X3, ABC expects to realize no tax benefit related to the $5,000,000 of reversing deductible temporary differences since they simply increase the amount of an NOL. Its expected income tax rate for

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20X3 would be 0% and ABC would have $0 admitted adjusted gross DTAs under paragraph 11.b.i. However, if some or all of the reversing temporary differences could be absorbed in the carryback period, ABC would have an admitted adjusted gross DTA under paragraph 11.a.[33(178)] The adjusted gross DTAs of $1,750,000 ($5,000,000 x 35%), related to ABC's reversing temporary differences, would also be available as part of its total adjusted gross DTAs, after reduction for adjusted gross DTAs admitted under paragraphs 11.a. and 11.b., that can be offset against gross DTLs in the paragraph 11.c. calculation.

6.14 If a company qualified to utilize the three-year applicable period under paragraph 11.b.i. and within that applicable period forecasted a taxable loss in one or more of the years and taxable income in the other years, the loss may be utilized in determining the with and without calculation. This loss utilization must be within the applicable period and would be limited to the amount allowed to be carried back or carried forward under applicable tax law.

7. Q – SSAP No. 101 provides that a reporting entity may admit deferred tax assets in an amount equal to federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, including any amounts established in accordance with the provisions of SSAP No. 5R as described in paragraph 3.a. of this statement related to those periods. What is the meaning of the term "taxes paid"? [Paragraph 11.a.]

7.1 A – Under paragraph 11.a. of SSAP No. 101, the term "taxes paid" means the total tax (both regular and AMT, but not including interest and penalties), that was or will be reported on the reporting entity's federal income tax returns for the periods included in the carryback period including any amounts established in accordance with the provision of SSAP No. 5R as described in paragraph 3.a. of SSAP No. 101 related to those periods. If a federal income tax return in the carryback period has been amended, or adjusted by the IRS, "taxes paid" would reflect the impact of the amended tax return, or settlement with the IRS.

7.2 In applying the term "taxes paid" to a reporting entity that is party to a consolidated federal income tax return, the term "taxes paid" means the total federal income tax (both regular and AMT) that was paid, or is expected to be paid to the common parent of the reporting entity's affiliated group, in accordance with the intercompany tax sharing agreement, with respect to the income tax years included in the carryback period. "Taxes paid" includes amounts established in accordance with the provision of SSAP No. 5R as described in paragraph 3.a. of SSAP No. 101 related to those periods, including current federal income taxes payable (i.e., accrued in the entity's financial statements) related to the carryback period. The ability of the reporting entity to recover (through loss carrybacks) taxes that were paid to its common parent is generally governed by the terms and provisions of the affiliated group's intercompany tax sharing or tax allocation agreement.

8. Q – How is a company's computation of adjusted gross and admitted adjusted gross deferred tax assets impacted if it joins in the filing of a consolidated federal income tax return? [paragraphs 7, 11, 12 and 16]

8.1 A – For purposes of determining the amount of DTAs and the amount admitted under paragraph 11, the calculation should be made on a separate company, reporting entity basis. Under paragraph 7, a

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reporting entity's gross deferred tax assets and liabilities are determined by identifying its temporary differences. These temporary differences are measured using a "balance sheet" approach by comparing statutory and tax basis balance sheets for that entity. Once a reporting entity determines its gross DTAs, they are reduced for any statutory valuation allowance adjustment that may be necessary to determine the adjusted gross DTAs. The amount of adjusted gross DTAs that are admitted is determined in accordance with paragraph 11.

8.2 Under paragraph 11.a., an entity shall determine the amount of "federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years." Such amount shall include any amounts established for tax loss contingencies in accordance with paragraph 3.a. Consistent with guidance promulgated in other EAIWG interpretations, a reporting entity that files a consolidated federal income tax return with its parent should look to the amount of taxes it paid (or were allocable to it) as a separate legal entity in determining the admitted adjusted gross DTAs under paragraph 11.a. Furthermore, the admitted adjusted gross DTAs under paragraph 11.a. may not exceed the amount that the entity could reasonably expect to have refunded by its parent (paragraph 12.c.). The taxes paid by the reporting entity represent the maximum DTAs that may be admitted under paragraph 11.a., although the amount could be reduced pursuant to the group's tax allocation agreement.

8.3 The amount of admitted adjusted gross DTAs under paragraph 11.b.i. is limited to the amount that the reporting entity expects to realize within the applicable period (refer to the 11.b.i. column of the applicable Realization Threshold Limitation Table in paragraph 11.b.) following the balance sheet date on a separate company basis. The entity must estimate its separate company taxable income and the tax benefit that it expects to receive from reversing deductible temporary differences in the form of lower tax payments to its parent. If the reporting entity has reversing adjusted gross DTAs during the applicable period for which it does not expect to realize a benefit under paragraph 11.b. on a separate company basis, the reporting entity cannot admit an amount related to such DTAs under paragraph 11,b., even though the reporting entity may be paid a tax benefit for such items pursuant to its tax allocation agreement.

8.4 The following examples reflect this analysis and assume that the surplus limitation of paragraph 11.b.ii. is not applicable:

Example 1:

8.5 Assume Company A, a life insurance company, joins in the filing of a consolidated federal income tax return. Consolidated taxes paid in prior carryback years total $150, of which Company A paid $100. Company A has existing temporary differences that reverse by the end of the third calendar year following the balance sheet date[34(179)] that, on a separate company reporting entity basis and following the applicable carryback provisions of the Internal Revenue Code for each year in which temporary differences reverse, would give rise to a tax recovery of $125.

8.6 Under paragraph 11.a., Company A could record an admitted DTA of $100, equal to the taxes it paid. Additionally, under paragraph 11.b.i., Company A could admit an additional $25, assuming it expects to realize such tax benefit based on its separate company analysis. Due to the consolidated return

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filing, the $100 admitted under paragraph 11.a. could only be admitted provided this amount could reasonably be expected to be refunded by the parent [paragraph 12.c.] and would be available pursuant to a written income tax allocation agreement [paragraph 16.b.].

Example 2:

8.7 Assume the same facts as in Example 1, except consolidated taxes paid in prior carryback years that could be recovered are $70 and, pursuant to a written income tax allocation agreement, taxes recoverable through loss carrybacks may not exceed consolidated taxes paid in prior carryback years.

8.8 In this situation, Company A would admit a DTA of $70 under paragraph 11.a. (recoverable taxes limited to consolidated taxes paid which could be refunded by the parent). In addition, $55 ($125-$70) of DTA may be admitted under paragraph 11.b.i., if Company A expected to realize this tax benefit on the basis of its separate company estimated taxable income and temporary differences that are expected to be realized within the applicable period following the balance sheet date.

Example 3:

8.9 Parent Company P files a consolidated federal income tax return with its insurance subsidiaries, R, S and T. Assume consolidated taxes that could be recovered through loss carryback total $450. However, in the prior carryback years $200 was paid by each of the subsidiaries, R, S and T. The difference between the amount paid by the subsidiaries ($600) and the amount available through loss carryback ($150) is attributable to interest expense incurred by Company P. Pursuant to the group's written income tax allocation agreement, in the case of loss carrybacks, taxes recoverable are limited to the consolidated taxes paid in the carryback years.

8.10 Because the adjusted gross DTA admitted under paragraph 11.a. for each reporting entity cannot exceed what each entity paid and could reasonably be expected to be refunded by P, no more than $450 in total may be admitted by the subsidiaries (under paragraph 11.a.). If the adjusted gross DTA associated with the subsidiaries' temporary differences that reverse in the 11.a. period exceed the $450 of taxes recoverable through loss carryback on a consolidated basis, the adjusted gross DTA admitted by the insurance subsidiaries under paragraph 11.a. should be allocated among the subsidiaries, consistent with the principles of its written income tax allocation agreement. This allocation would, in most instances, be based on each subsidiary's share of reversing temporary differences.

8.11 Under paragraph 11.c., an entity may admit its adjusted gross DTAs, after application of paragraphs 11.a. and 11.b., based upon offset against its own existing gross DTLs and not against gross DTLs of other members of the affiliated or consolidated group.

9a. Q – Current income taxes are defined by paragraph 3.a. to include tax loss contingencies for current and all prior years, computed in accordance with SSAP No. 5R, including the modifications in paragraphs 3.a.i, 3.a.ii. and 3.a.iii. How does the modification provided in paragraph 3.a.iii. impact the calculation of the tax contingencies recorded?

9.1 A – Paragraph 3.a.iii. provides the following rule: If the estimated tax loss contingency is greater

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than 50% of the tax benefit originally recognized, the tax loss contingency recorded shall be equal to 100% of the original tax benefit recognized.

9.2 For example, assume that a company claimed a deduction in its current year federal income tax return that resulted in a $100 permanent tax benefit[35(180)]. Management must assume that the tax position will be examined by a taxing authority that has full knowledge of all relevant information (paragraph 3.a.ii.). In addition, management has determined that the probability of a liability is more likely than not (a likelihood of more than 50% pursuant to paragraph 3.a.i.) and that the liability can be reasonably estimated. Management's best estimate of the loss of the tax benefit is $40 (an amount not greater than 50% of the tax benefit originally recognized). Under these facts, the company would establish a current tax liability in the amount of $40, increasing its current income tax expense by $40.

DR	Current income tax expense	$40	
CR	Liability for current income tax		$40

9.3 Assume the same facts as 9.2, except that management determines the best estimate of the liability to be $60 (an amount greater than 50% of the tax benefit originally recorded). Under paragraph 3.a.iii., the company would be required to record a tax contingency of $100 offsetting the entire original tax benefit recorded. Under these facts, the company would establish a current tax liability in the amount of $100, increasing its current income tax expense by $100.

DR	Current income tax expense	$100	
CR	Liability for current income tax		$100

9b. Q – What impact, if any, does the inclusion of tax contingencies as a component of current income taxes have on the determination of deferred income taxes? [Paragraph 3.c.]

9.4 A – The purpose of this interpretation is to address when such contingencies should be "grossed-up" and reflected in the calculation of both statutory current and deferred federal income taxes.

9.5 Gross deferred tax assets and liabilities are determined in accordance with paragraph 7 of SSAP No. 101, and reflect the changes in temporary differences taken into account in estimating taxes currently payable and are manifested in the enterprise's tax basis balance sheet. If gross tax loss contingencies associated with temporary differences have been included in taxes currently payable, a corresponding adjustment must be made to the tax basis balance sheet used in the determination of gross deferred tax assets and liabilities. Deferred tax assets and liabilities are not adjusted for tax contingencies not associated with temporary differences (i.e. permanent differences).

9.6 For example, assume that a company determines, in accordance with SSAP No. 5R, including the modifications in paragraph 3.a. of SSAP No. 101, a tax loss contingency is required to be established for a $100 deduction claimed in a prior year federal income tax return. Assuming a 35% tax rate, the company would establish a current tax liability in the amount of $35, increasing its current income tax

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expense by $35.

DR	Current income tax expense	$35	
CR	Liability for current income tax		$35

9.7 If the $100 deduction was associated with a temporary difference such as reserves, the company would make a corresponding adjustment to deferred taxes. The company would increase its gross deferred tax asset for reserves by $35 to reflect the future tax benefit associated with that reserve deduction. Any gross deferred tax asset recorded would still be subject to the admissibility requirements of paragraph 11.

DR	Gross deferred tax asset	$35	
CR	Change in net deferred tax (surplus)		$35

9.8 If the $100 deduction was associated with a permanent item such as meals and entertainment expenses, the company would make no corresponding adjustment to the deferred tax assets.

9.9 In determining the timing of when a tax loss contingency for a temporary item should be grossed up, paragraph 3.c. of SSAP No. 101 provides the following guidance:

> 3.c. In determining when tax loss contingencies associated with temporary differences should be included in current income taxes under Paragraph 3.a., and therefore included in deferred taxes under paragraph 7, a reporting entity is not required to "gross-up" its current and deferred taxes until such time as an event has occurred that would cause a re-evaluation of the contingency and its probability of assessment, e.g., the IRS has identified the item as one which may be adjusted upon audit. Such an event could be the reporting entity's (or its affiliate or parent in a consolidated income tax return) receipt of a Form 5701, Proposed Audit Adjustment, or could occur earlier upon receipt of an Information Document Request. At such time, the company must reassess the probability of an adjustment, reasonably re-estimate the amount of tax contingency as determined in accordance with paragraph 3.a., make any necessary adjustment to deferred taxes, and re-determine the admissibility of any adjusted gross deferred tax asset as provided in paragraph 11.

10a. Q – If the reporting entity adjusts the amount of regular taxable income and capital gains reported on a prior year income tax return from the amount originally determined for financial reporting purposes, how is the effect of the change reported in the current year? [Paragraph 19]

10.1 A – Paragraph 19 of SSAP No. 101 indicates that "income taxes incurred or received during the current year attributable to prior years shall be allocated, to the extent not previously provided, to net income in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* (SSAP No. 3) unless attributable, in whole or in part, to realized capital gains or losses, in which case, such amounts shall be apportioned between net income and realized capital gains and losses, as appropriate". Paragraph 19 also indicates that income taxes incurred are to be allocated to ordinary income and realized capital

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gains consistent with paragraph 38 of FAS 109. Paragraph 38 of FAS 109 provides, in general, that the portion of the total income tax expense remaining after allocation to ordinary income would be allocated to realized capital gains or losses.

10.2 In accordance with paragraph 19, the amount of additional federal income taxes incurred in the current year with respect to the prior year would be allocated between ordinary income and realized capital gain items. The amount of additional federal income tax expense allocated to ordinary income should be determined by comparing the amount of additional tax expense actually incurred to the amount of tax expense that would have been incurred had the adjustment to ordinary income been zero (a "with and without" computation). The remaining amount of additional federal income tax expense would then be allocated to realized capital gains. The amounts of additional federal income tax expense allocated to ordinary income and realized capital gains would be included in the current period's federal income tax expense and not as a direct adjustment to surplus.

10.3 As an example, assume Company X files its 20X1 federal income tax return and reports $1,000,000 of taxable income comprised of $800,000 of ordinary income and $200,000 of capital gain income. Since the company is subject to taxation at a 34 percent tax rate on all its income, it incurred federal income tax expense of $340,000. In preparing its 20X1 statutory income tax provision, the company estimated that its liability for 20X1 federal income tax would be $238,000 based on $600,000 of ordinary income and $100,000 realized capital gains.

10.4 In determining the amount of "income taxes incurred" for its 20X2 financial statement, Company X must include the additional $102,000 of income tax expense incurred on its 20X1 federal income tax return ($340,000 actual tax incurred less $238,000 originally reported) in net income for 20X2 pursuant to paragraph 19 of SSAP No. 101 and not as a surplus adjustment. The $102,000 additional expense would be allocated to federal income taxes on net income and realized capital gains and losses as follows:

Total additional income tax expense	$102,000
Tax expense allocated to operations ($200,000 additional income x 34%)	68,000
Tax expense allocated to realized gains	$ 34,000

The tax expense allocated to operations was determined as follows:

Total recomputed tax expense	$340,000
Tax expense with only capital gain changes	272,000[36(181)]
Tax expense allocated to operations	$ 68,000

10.5 For all purposes of computing and allocating federal income taxes between operations and capital gains and losses, the character of the income or loss item as determined for statutory accounting

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purposes should be followed. Thus, if an income item is treated as a capital gain for statutory accounting purposes but as ordinary income for tax purposes, the federal income tax allocable to such income would be considered tax expense attributable to capital gains.

10b. Q – What is meant by the phrase in paragraph 18 "a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL"? [Paragraph 18]

10.6 A – Pursuant to Paragraph 18 of SSAP No. 101, a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL in accordance with paragraph 35 of FAS 109. Paragraph 35 of FAS 109 indicates that income taxes incurred are to be allocated between various items, including gains from operations and items charged or credited directly to shareholders' equity, such as the change in unrealized gains and losses.

10.7 To the extent a reporting entity's admitted DTA or its DTL changes during the year, the portion of such change allocable to changes in unrealized gains and losses during the year should be determined. The portion so allocable would be reported with, and netted against, the related change in unrealized gains and losses reported as a component of changes in surplus. The remaining portion of the change in DTA or DTL allocable to other temporary differences should be reported as a separate component of changes in surplus and/or change in nonadmitted assets.

10.8 For example, assume the reporting entity has DTAs of $1,000 relating to temporary differences other than unrealized losses, and a $100 DTL relating to unrealized gains as of the beginning of the year. Since the entity is subject to tax at 35 percent and all of its DTAs are expected to reverse within one year, the entity recorded a $900 net admitted DTA as of the beginning of the year.

10.9 During the current year, the DTAs relating to temporary differences other than unrealized losses did not change, but the DTL relating to the entity's unrealized gains increased by $100 (unrealized gains increased by $285 during the year). As a result, the amount of the entity's net admitted DTAs decreased by $100.

10.10 Pursuant to paragraph 18 of SSAP No. 101, the $100 decrease in the DTA during the year is to be allocated between changes attributable to temporary differences other than unrealized gains and losses and those attributable to unrealized gains and losses. Since the DTA relating to temporary differences other than unrealized gains and losses did not change during the year, the entire decrease is allocable to the change in unrealized gains. Therefore, the $100 decrease is to be allocated and netted against the $285 change in unrealized gains reported in change in surplus, resulting in a $185 net increase in surplus relating to its unrealized gains. If a portion of the unrealized loss DTA is determined to be nonadmitted, that amount is not recorded separately from the operating differences DTA. The change in the total nonadmitted DTA from period to period is recorded in surplus as a Change in Nonadmitted Assets.

11. Q – How are current and deferred income taxes to be accounted for in interim periods? [Paragraphs 12.d. and 20]

11.1 A – In setting forth the methodology for the computation of current income taxes (income taxes

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incurred) in interim periods, paragraph 20 states:

> 20. Income taxes incurred in interim periods shall be computed using an estimated annual effective current tax rate for the annual period in accordance with the methodology described in paragraphs 19 and 20 of *Accounting Principles Board Opinion No. 28, Interim Financial Reporting*. Estimates of the annual effective tax rate at the end of interim periods are, of necessity, based on estimates and are subject to subsequent refinement or revision. If a reliable estimate cannot be made, the actual effective tax rate for the year-to-date may be the best estimate of the annual effective tax rate. If an insurer is unable to estimate a part of its "ordinary" income (or loss) or the related tax (or benefit) but is otherwise able to make a reliable estimate, the tax (or benefit) applicable to the item that cannot be estimated shall be reported in the interim period in which the item is reported.

11.2 As a result, to the extent a reliable estimate can be made of an expected annual effective tax rate, reporting entities should apply this rate to net income before federal and foreign income taxes, in the case of property and casualty insurers and health insurers, and net income and realized capital gains before federal and foreign income taxes in the case of life insurers. If a reliable estimate of the expected annual effective tax rate cannot be made, reporting entities should compute current and deferred taxes at interim reporting dates using the most reliable information that is available.

11.3 The following examples illustrate the estimation process for income taxes incurred using the estimated annual effective rate:

Projected statutory net income[37(182)] for current year		$10,000,000
Estimated annual permanent differences		(2,800,000)
Estimated annual temporary differences:		2,000,000
Projected taxable income for current year		$9,200,000
Projected federal tax for current year (at 35%)		$3,220,000
Estimated annual effective tax rate		32.2%

11.4 As a result, assuming that during the calendar year the reporting entity's expectations as to its statutory and taxable income do not change, income tax incurred will be recorded on a quarterly basis as follows:

Quarter	**Statutory Income (Loss)**	**Income Taxes Incurred**
1	$(2,000,000)	$(644,000)
2	4,000,000	1,288,000

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3	6,000,000	1,932,000
4	2,000,000	644,000
Total	$10,000,000	$3,220,000

11.5 If the reporting entity's expectations as to its statutory and taxable income change in the second quarter so that it expects that its annual effective rate will increase from 32.2% to 34%, it will record income taxes incurred in the second quarter of $1,324,000 (cumulative statutory income at end of the second quarter of $2,000,000 at 34% or $680,000 less $644,000 tax benefit recorded in first quarter).

11.6 As noted above, life insurers must estimate their annual effective tax rate and record income taxes incurred based on net income and realized capital gains before federal and foreign income taxes. With regard to intraperiod tax allocation, paragraph 19 states in relevant part:

> 19. Income taxes incurred shall be allocated to net income and realized capital gains or losses in a manner consistent with paragraph 38 of FAS 109.

11.7 As a result of the above and where the reporting entity expects realized capital gains or losses for the annual period, income taxes incurred must be allocated using a "with and without" methodology to net income before taxes and realized capital gains (see Question 10.4 for further discussion).

11.8 An example of this "with and without" methodology is as follows:

Projected statutory net income for current year		$10,000,000
Realized gains included above		(1,000,000)
		9,000,000
Estimated annual permanent differences:		(2,800,000)
Estimated annual temporary differences:		2,000,000
Projected ordinary taxable income for current year		$8,200,000
Projected ordinary federal tax for current year (at 35%)		$2,870,000
Projected capital gain federal tax for current year (at 35%)		350,000
Projected total federal tax for current year		$3,220,000
Estimated ordinary annual effective tax rate ($2,870,000 / $9,000,000)		31.9%
Estimated capital gain annual effective tax rate ($350,000 / $1,000,000)		35.0%
Estimated total annual effective tax rate ($3,220,000 / $10,000,000)		32.2%

11.9 As a result, assuming that during the calendar year the reporting entity's expectations as to its statutory and taxable income (including the amounts of ordinary and capital income) do not change,

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income tax incurred will be recorded on a quarterly basis as follows:

Quarter	Ordinary Income (Loss)	Capital Income (Loss)	Ordinary Taxes Incurred	Capital Taxes Incurred
1	$(1,000,000)	$(1,000,000)	$(319,000)	$(350,000)
2	3,000,000	1,000,000	956,000	350,000
3	5,000,000	1,000,000	1,595,000	350,000
4	2,000,000	0	638,000	0
Total	$9,000,000	$1,000,000	$2,870,000	$350,000

11.10 With respect to the recording of deferred taxes on an interim basis paragraph 12.d. states:

> 12.d. The phrases "reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years," "realized within one year of the balance sheet date" and "realized within three years of the balance sheet date" are intended to accommodate interim reporting dates and reporting entities that file on an other than calendar year basis for federal income tax purposes.

11.11 When considered in the context of paragraph 20, this paragraph requires the use of the annual effective rate when determining deferred taxes at an interim reporting date. As such, a reporting entity's admitted adjusted gross DTAs are determined in accordance with paragraph 11 by reference to the adjusted gross DTAs that will reverse each year in the applicable period. Note however, that due to the inherent unpredictability, and general inability to project changes in capital gains and losses on a quarter by quarter basis, the deferred tax implications of the changes in unrealized gains and losses should be recorded on a discrete period basis (i.e., based on the change in the amounts on a quarter by quarter basis). For example in determining its admitted adjusted gross DTAs at March 31, 20X2, the reversal period referred to above is calendar years 20X3, 20X4 and 20X5 (i.e., expected adjusted gross DTAs at December 31, 20X2 that are expected to reverse in 20X3, 20X4 and 20X5).

11.12 This methodology is illustrated by the following example:

In this example, XYZ Co. is a life insurance company[38(183)] that has a three-year carryback potential and also has an ExDTA ACL RBC percentage of 700%.

Projected statutory net income for 20X3		$10,000,000
Estimated annual permanent differences:		(2,800,000)
Estimated annual temporary differences:		2,000,000
Projected ordinary taxable income for current year		$9,200,000
Temporary differences at December 31, 20X2:		$5,000,000

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Estimated temporary differences at December 31, 20X3:			$7,000,000
Taxable income in carryback period (taxes paid at 35%):			
	Year ended December 31, 20X0	$800,000	($280,000)
	Year ended December 31, 20X1	2,000,000	(700,000)
	Year ended December 31, 20X2	3,000,000	(1,050,000)
	Year ended December 31, 20X3	$9,200,000	($3,220,000)

Note: Year ended December 31, 20X3 taxable income and taxes paid considered in the calculation of its interim tax accruals are based on the reporting entity's estimate of its annual taxable income and taxes to be paid. This amount may differ from the quarterly federal income tax estimates it expects to make during the year.

	Reversing Period		
	20X3	20X4	20X5
December 31, 20X2 Temporary difference reversals:	$2,000,000	$1,500,000	$1,500,000
	20X4	20X5	20X6
December 31, 20X3 Temporary difference reversals:	$3,000,000	$2,000,000	$2,000,000

Admitted deferred tax assets at December 31, 20X2:				
	Paragraph 11.a.			
		20X0	$800,000	
		20X1	2,000,000	
		20X2	2,200,000	
			5,000,000	
		Taxes paid at 35%		$1,750,000
	Paragraph 11.b.			0
	Paragraph 11.c.			0
	Total admitted			$1,750,000

Note: The recovery of federal income taxes paid in prior years under paragraph 11.a. is calculated in this example by carrying back 20X3's temporary difference reversals to offset 20X0's taxable income of $800,000 and $1,200,000 of 20X1's taxable income; then carrying back 20X4's temporary difference reversals to offset 20X1's remaining taxable income of $800,000 and $700,000 of 20X2's taxable income; finally, carrying back 20X5's temporary difference reversals to offset $1,500,000 of 20X2's

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taxable income. Since all gross DTAs were admitted under paragraph 11.a., paragraphs 11.b. and 11.c. need not be considered.				
Admitted deferred tax assets at December 31, 20X3:				
	Paragraph 11.a.			
		20X1	$2,000,000	
		20X2	3,000,000	
		20X3	2,000,000	
			7,000,000	
		Taxes paid at 35%		$2,450,000
	Paragraph 11.b.			0
	Paragraph 11.c.			0
	Total admitted			$2,450,000
Note: The recovery of federal income taxes paid in prior years under paragraph 11.a. is calculated in this example by carrying back 20X4's temporary difference reversals to offset 20X1's taxable income of $2,000,000 and $1,000,000 of 20X2's taxable income; then carrying back 20X5's temporary difference reversals to offset 20X2's remaining taxable income of $2,000,000; finally, carrying back 20X6's temporary difference reversals to offset $2,000,000 of 20X3's taxable income. Since all gross DTAs were admitted under paragraph 11.a., paragraphs 11.b. and 11.c. need not be considered.				
Total estimated federal taxes for 20X3:				
	Income taxes incurred (current tax) ($9,200,000 X 35%)			$3,220,000
	Change in deferred tax ($1,750,000 – $2,450,000)			(700,000)
				$2,520,000

11.13 As a result of the above, the annual effective tax rate for current and deferred income taxes is as follows:

Current ($3,220,000/$10,000,000)	32.2%
Deferred (($700,000)/$10,000,000)	(7.0)%
Total annual effective rate	25.2%

Quarter	**Statutory Income (Loss)**	**Income Taxes Incurred**	**Deferred Taxes**
1	$(2,000,000)	$(644,000)	$140,000

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2	4,000,000	1,288,000	(280,000)
3	6,000,000	1,932,000	(420,000)
4	2,000,000	644,000	(140,000)
Total	$10,000,000	$3,220,000	$(700,000)

11.14 To the extent that a reporting entity's estimated year end[39(184)] admitted adjusted gross deferred tax assets are limited by its surplus pursuant to paragraph 11.b.ii., the annual effective deferred tax rate must be adjusted to consider the impact of this limitation on a quarterly basis.

12. Q – How do you present deferred taxes in the Annual Statement? [Paragraphs 8, 18, 21-28 and 36]

12.1 A – This answer is divided into four different parts.

Change in Accounting Principle

12.2 As required by paragraph 37 of SSAP No. 101, balances of current and deferred federal and foreign income taxes resulting from the adoption of SSAP No. 101 effective January 1, 2012 shall be presented in the Annual Statement as a Cumulative Effect of Changes in Accounting Principles. SSAP No. 3 provides the following:

> 3. A change in accounting principle results from the adoption of an accepted accounting principle, or method of applying the principle, which differs from the principles or methods previously used for reporting purposes. A change in the method of applying an accounting principle shall be considered a change in accounting principle.
>
> 4. A characteristic of a change in accounting principle is that it concerns a choice from among two or more statutory accounting principles. However, a change in accounting principle is neither (a) the initial adoption of an accounting principle in recognition of events or transactions occurring for the first time or previously immaterial in their effect, nor (b) the adoption or modification of an accounting principle necessitated by transactions or events that are clearly different in substance from those previously occurring.
>
> 5. The cumulative effect of changes in accounting principles shall be reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle. The cumulative effect is the difference between the amount of capital and surplus at the beginning of the year and the amount of capital and surplus that would have been reported at that date if the new accounting principle had been applied retroactively for all prior periods.

12.3 In accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors* (SSAP No. 3), adjustments to amounts recorded as of January 1, 2012, would be recorded as a modification to the changes in accounting principle account rather than corrections of an error through the period of 2012.

Illustration A Assumptions:

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12.4 On January 1, 2012, as a result of applying paragraph 11.b. requirements to use current period statutory capital and surplus rather than prior quarter statutory capital and surplus as required by previous guidance, the AlphaBeta P/C Company computed the following balances related to deferred taxes:

	1/1/12	**12/31/11**
Gross DTA	$200,000	$200,000
Statutory Valuation Allowance Adjustment	0	0
Adjusted Gross DTA	200,000	200,000
Deferred Tax Assets Nonadmitted	25,000	10,000
Admitted Adjusted Gross DTA	175,000	190,000
Gross DTL	100,000	100,000
Net Admitted Adjusted Gross DTA	$75,000	$90,000

There was no change in the amount of the current tax liability recorded by AlphaBeta as a result of the adoption of SSAP No. 101.

12.5 The Cumulative Effect of Changes in Accounting Principles line shown in the surplus section of the Annual Statement would show a decrease of $15,000 ($90,000 – $75,000) on 1/1/2012. In addition, during the second quarter of 2012, the Company determined that it incorrectly computed its Net Admitted Adjusted Gross DTA as of 1/1/2012 under SSAP No. 101 and modified its opening balance as follows (note that modifications were not a result of changes in circumstances or events which occurred during 2012):

	Revised 1/1/12
Gross DTA	$200,000
Statutory Valuation Allowance Adjustment	0
Adjusted Gross DTA	200,000
DTA Nonadmitted	35,000
Admitted Adjusted Gross DTA	165,000
Gross DTL	100,000
Net Admitted Adjusted Gross DTA	$65,000

12.6 The Company would record the following balances in its 3/31/12 financial statements:

	1/1/12	**Revised 1/1/12**	**Increase (Decrease)**
Gross DTA	$200,000	$200,000	$0
Statutory Valuation Allowance Adjustment	0	0	0

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Adjusted Gross DTA	200,000	200,000	0
DTA Nonadmitted	25,000	35,000	10,000
Admitted Adjusted Gross DTA	175,000	165,000	(10,000)
Gross DTL	100,000	100,000	0
Net Admitted Adjusted Gross DTA	$75,000	$65,000	($10,000)

12.7 The additional $10,000 decrease in net admitted adjusted gross DTA would also be recorded through the Cumulative Effect of Changes in Accounting Principles line shown in the surplus section of the Annual Statement.

Unrealized Capital Gains and Losses

12.8 SSAP No. 101 paragraph 18 states:

> 14. In accordance with paragraph 35 of FAS 109, a reporting entity's unrealized gains and losses shall be recorded net of any allocated DTA or DTL. The amount allocated shall be computed in a manner consistent with paragraph 38 of FAS 109.

12.9 The following illustrates the presentation of such requirement in the Annual Statement:

Illustration B Assumptions:

12.10 Entity grouped its investments in a reasonable and consistent manner and calculated the following gross amounts attributable to appreciation and depreciation in the fair value of its common stocks during 20X2 (see question 2 regarding grouping of assets and liabilities for measurement):

	Gross	**Carrying Value**	**Rate**	**Tax Effected DTA (DTL)**
Common stock carrying value 1/1/X2		$800,000		
Unrealized (loss)	($428,571)		35%	$150,000
Unrealized gain	342,857		35%	(120,000)
Net (loss) gain		(85,714)		$30,000
Common stock carrying value 12/31/X2		$714,286		

12.11 The journal entries need to present unrealized losses and gains net of tax are:

12/31/X2	DR	Change in unrealized capital gains and losses	$85,714
	CR	Common stock	($85,714)
	Recognition of net depreciation in FV of common stock		

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12/31/X2	DR	Deferred tax asset	$150,000
	CR	Deferred tax liability	($120,000)
	CR	Change in deferred income taxes	($30,000)
	Recognition of gross deferred tax amounts		

12/31/X2	DR	Change in deferred income taxes	$30,000
	CR	Change in unrealized capital gains and losses	($30,000)
	Reclass tax effect of net unrealized loss per paragraph 18 of SSAP No. 101		

12.12 Condensed 12/31/X2 Balance Sheet:

ASSETS	**20X2**	**20X1**		**LIABILITIES, SURPLUS AND OTHER FUNDS**	**20X2**	**20X**
Common Stock	$714,286	$800,000		Surplus:		
Net deferred tax asset	30,000			Beginning of year	$800,000	
				Change in UNL	(55,714)[40(185)]	
Total Assets	$744,286	$800,000		**Liabilities & Surplus**	$744,286	$80(

Annual Statement Presentation

12.13 In accordance with SSAP No. 101, DTAs and DTLs shall be offset and presented as a single amount on the statement of financial position. The following illustrates this requirement:

Illustration C Assumptions:

12.14 The entity had the following balances (1/1/X2 balances carried forward from Illustration A):

	1/1/X2	**12/31/X2**	**Change**
Gross DTA	$200,000	$510,000	$310,000
Statutory Valuation Allowance Adjustment	0	10,000	10,000
Adjusted Gross DTA	200,000	500,000	300,000[41(186)]
DTA Nonadmitted	25,000	150,000	125,000
Admitted Adjusted Gross DTA	175,000	350,000	175,000
Gross DTL	100,000	200,000	100,000
Net Admitted Adjusted Gross DTA	$75,000	$150,000	$75,000

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Current FIT Recoverable	**$18,000**	**$20,000**	**$2,000**

12.15 Illustrative 12/31/X2 Balance Sheet for Illustration C:

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
Current Federal and foreign income tax recoverable and interest thereon	$20,000	$0	$20,000	$18,000
Net deferred tax asset	$300,000	$150,000	$150,000	$75,000

12.16 Illustrative 12/31/X2 Income Statement for Illustration C:

STATEMENT OF INCOME (P/C) **SUMMARY OF OPERATIONS (Life & Health)** **STATEMENT OF REVENUES AND EXPENSES (Health)**	1 Current Year	2 Prior Year
Gains and (losses) in surplus		
Change in net unrealized capital gains (losses) less capital gains tax of $	($55,714)	0
Change in net deferred income tax	$170,000	0
Change in nonadmitted assets	($125,000)	0

12.17 Illustrative 12/31/X2 Exhibit of Nonadmitted Assets for Illustration C:

	1 End of Current Year	2 End of Prior Year	3 Changes for Year (Increase) Decrease
Net deferred tax asset	$150,000	$25,000	($125,000)
Total	$150,000	$25,000	($125,000)

Illustration D Assumptions:

12.18 The entity had the following balances (1/1/20X2 balances carried forward from Illustration A):

	1/1/X2	**12/31/X2**	**Change**
Gross DTA	$200,000	$510,000	$310,000
Statutory Valuation Allowance Adjustment	0	10,000	10,000

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Adjusted Gross DTA	200,000	500,000	300,000 42(187)
DTA Nonadmitted	25,000	150,000	125,000
Net Admitted Adjusted Gross DTA	175,000	350,000	175,000
Gross DTL	100,000	200,000	100,000
Net Admitted Adjusted Gross DTA	$75,000	$150,000	$75,000
Current FIT Liability	**$7,000**	**$12,000**	**$5,000**

12.19 Illustrative 12/31/X2 Balance Sheet for Illustration D:

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
Net deferred tax asset	$300,000	$150,000	$150,000	75,000

LIABILITIES, SURPLUS AND OTHER FUNDS	1 Current Year	2 Prior Year
Current Federal and foreign income taxes (including $0 on realized capital gains (Losses))	$12,000	$7,000

12.20 Illustrative 12/31/X2 Income Statement for Illustration D:

STATEMENT OF INCOME (P/C) **SUMMARY OF OPERATIONS (Life & Health)** **STATEMENT OF REVENUES AND EXPENSES (Health)**	1 Current Year	2 Prior Year
Gains and (losses) in surplus		
Change in net unrealized capital gains (losses) less capital gains tax of $	($55,714)	0
Change in net deferred income tax	$170,000	0
Change in nonadmitted assets	($125,000)	0

12.21 Illustrative 12/31/X2 Exhibit of Nonadmitted Assets for Illustration D:

	1 End of Current	2 End of	3 Changes for Year (Increase)

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	Year	Prior Year	Decrease
Net deferred tax asset	$150,000	$25,000	($125,000)
Total	$150,000	$25,000	($125,000)

Notes to the Financial Statements Disclosures:

12.22 SSAP No. 101 paragraphs 21-28 include extensive disclosure requirements. Although some of these amounts are presented on the face of the financial statements or in schedules or exhibits to the Annual Statement, they will be included in the Notes to the Financial Statements both in the Annual Statement and in the Annual Audited Financial Statements.

12.23 This section provides specific examples that illustrate the disclosures required in SSAP No. 101. The formats in the illustrations are not requirements. Some of the disclosure paragraphs of SSAP No. 101 are not specific as to whether the entity should disclose the nature of certain items or whether the entity should disclose specific amounts. The illustrations included herein use a combination of each method. The NAIC encourages a format that provides the information in the most understandable manner in the specific circumstances. The following illustrations are for a single hypothetical insurance enterprise, referred to as AlphaBeta Property & Casualty Insurance Company.[43(188)]

12.24 All of the disclosures would be completed in the year-end Annual Statement and audited statutory financial statements. The disclosures of paragraphs 22-24 and 25 (on a prospective basis) and 26-28 should be presented in accordance with paragraph 64 of the Preamble on the initial adoption of SSAP No. 10, a predecessor of SSAP No. 101, therefore these notes would only be presented in the first, second and third Quarterly Statements if the underlying data changed significantly.

12.25 Selected AlphaBeta P/C Company Financial Data at December 31, 20X2 (Balance Sheet information carried forward from Illustration C):

ASSETS	Current Year			Prior Year
	1 Assets	2 Nonadmitted Assets	3 Net Admitted Assets (Cols. 1 - 2)	4 Net Admitted Assets
Current federal and foreign income tax recoverable and interest thereon	$20,000	$0	$20,000	$18,000
Net deferred tax asset	$300,000	$150,000	$150,000	$75,000

CAPITAL AND SURPLUS ACCOUNT	1 Current Year	2 Prior Year
Change in net unrealized capital gains (losses)less capital gains tax of $30,000	($55,714)	0

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Change in net deferred income tax	$170,000	0
Change in nonadmitted assets	($125,000)	0

EXHIBIT OF NONADMITTED ASSETS	1 End of Current Year	2 End of Prior Year	3 Changes for Year (Increase) Decrease
Net deferred tax asset	$150,000	$25,000	($125,000)

STATEMENT OF INCOME	**20X2**
UNDERWRITING INCOME	
Premiums earned	$5,250,000
DEDUCTIONS:	
Losses incurred	3,550,000
Loss adjustment expenses incurred	1,750,000
Other underwriting expenses incurred	525,000
Net underwriting gain (loss)	(575,000)
INVESTMENT INCOME	
Net investment gain (loss)	1,350,000
OTHER INCOME	
Total other income	125,000
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	900,000
Dividends to policyholders	200,000
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	700,000
Federal and foreign income taxes incurred	220,000
Net income	$480,000

Paragraph 22 Illustration:

12.26 The components of the net DTA recognized in the Company's Assets, Liabilities, Surplus and Other Funds are as follows:

	12/31/20X2			12/31/20X1			
	Ordinary	Capital	Total	Ordinary	Capital	Total	Ordina

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	12/31/20X2			12/31/20X1			
Gross Deferred Tax Assets	$375,000	$135,000	$510,000	$93,000	$107,000	$200,000	$282
Statutory Valuation Allowance Adjustments	0	10,000	10,000	0	0	0	
Adjusted Gross Deferred Tax Assets	375,000	125,000	500,000	93,000	107,000	200,000	282
Deferred Tax Assets Nonadmitted	150,000	0	150,000	20,000	5,000	25,000	130
Subtotal Net Admitted Deferred Tax Asset	225,000	125,000	350,000	73,000	102,000	175,000	152
Deferred Tax Liabilities	21,000	179,000	200,000	15,000	85,000	100,000	6
Net Admitted Deferred Tax Asset/(Net Deferred Tax Liability)	$204,000	($54,000)	$150,000	$58,000	$17,000	$75,000	$146
Admission Calculation Components SSAP No. 101 (Paragraph 11)							
a. Federal Income Taxes Paid In Prior Years Recoverable Through Loss Carrybacks.	$85,000	$5,000	$90,000	$45,000	$5,000	$50,000	$40
b. Adjusted Gross Deferred Tax Assets Expected To Be Realized (Excluding The Amount Of Deferred Tax Assets From a, above) After Application of the Threshold Limitation. (The Lesser of b.i. and b.ii. Below)	50,000	10,000	60,000	13,000	12,000	25,000	37
i. Adjusted Gross Deferred Tax Assets Expected to be Realized Following the Balance Sheet Date.	**NA**	**NA**	**60,000**	**NA**	**NA**	**25,000**	
ii. Adjusted Gross Deferred Tax Assets Allowed per Limitation Threshold.	**NA**	**NA**	**900,000**	**NA**	**NA**	**750,000**	
c. Adjusted Gross Deferred Tax Assets (Excluding The Amount Of Deferred Tax Assets From a. and b. above) Offset by Gross Deferred Tax Liabilities.	90,000	110,000	200,000	15,000	85,000	100,000	75
Deferred Tax Assets Admitted as the result of application of SSAP No. 101.Total (a. + b. + c.)	$225,000	$125,000	$350,000	$73,000	$102,000	$175,000	$152
	20X2 Percentage	20X1 Percentage					
Ratio Percentage Used To Determine Recovery Period And Threshold Limitation Amount[44(189)]	600%	500%					

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	12/31/20X2			12/31/20X1			
Amount Of Adjusted Capital And Surplus Used To Determine Recovery Period And Threshold Limitation[45(190)]	$6,000,000	$5,000,000					
The Company's tax-planning strategies include the use of reinsurance-related tax-planning strategies.							
Impact of Tax Planning Strategies	12/31/20X2			12/31/20X1			
	Ordinary Percent	Capital Percent	Total Percent[46(191)]	Ordinary Percent	Capital Percent	Total Percent	Ordinar
Adjusted Gross DTAs (% of Total Adjusted Gross DTAs)	6%	7%	13%	7%	7%	14%	-
Net Admitted Adjusted Gross DTAs (% of Total Net Admitted Adjusted Gross DTAs)	14%	15%	29%	15%	15%	30%	-

Paragraph 23 Illustration:

12.27 The Company has not recognized a deferred tax liability of approximately $30,000 for the undistributed earnings of its 100 percent owned foreign subsidiaries that arose in 20X2 and prior years because the Company does not expect those unremitted earnings to reverse and become taxable to the Company in the foreseeable future. A deferred tax liability will be recognized when the Company expects that it will recover those undistributed earnings in a taxable manner, such as through receipt of dividends or sale of the investments. As of December 31, 20X2, the undistributed earnings of these subsidiaries were approximately $88,000.

Paragraph 24 Illustration:

12.28 The provisions for incurred taxes on earnings for the years ended December 31 are:

	20X2	**20X1**
Federal	$180,000	$135,000
Foreign	40,000	15,000
	220,000	150,000
Federal income tax on net capital gains	52,000	36,000
Utilization of capital loss carry-forwards	(52,000)	(36,000)
Federal and foreign income taxes incurred	$220,000	$150,000

12.29 The tax effects of temporary differences that give rise to significant[47(192)] portions of the deferred

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tax assets and deferred tax liabilities are as follows:

Deferred Tax Assets:	12/31/20X2	12/31/20X1	Change
Ordinary			
Discounting of unpaid losses	30,000	10,000	20,000
Unearned premium reserve	235,000	50,000	185,000
Investments	25,000	15,000	10,000
Pension accrual	65,000	15,000	50,000
Other (including items <5% of total ordinary tax assets)	20,000	3,000	17,000
Subtotal	375,000	93,000	282,000
Statutory valuation allowance adjustment	0	0	0
Nonadmitted	150,000	20,000	130,000
Admitted ordinary deferred tax assets	225,000	73,000	152,000
Capital			
Investments	125,000	45,000	80,000
Net capital loss carry-forward	10,000	62,000	(52,000)
Other (including items <5% of total capital tax assets)	0	0	0
Subtotal	135,000	107,000	28,000
Statutory valuation allowance adjustment	10,000	0	10,000
Nonadmitted	0	5,000	(5,000)
Admitted capital deferred tax assets	125,000	102,000	23,000
Admitted deferred tax assets	350,000	175,000	175,000
Deferred Tax Liabilities:			
Ordinary			
Investments	10,000	5,000	5,000
Fixed assets	6,000	5,000	1,000
Other (including items <5% of total ordinary tax liabilities)	5,000	5,000	0
Subtotal	21,000	15,000	6,000
Capital:			
Investments	110,000	55,000	55,000
Real estate	64,000	25,000	39,000
Other (including items <5% of total capital tax liabilities)	5,000	5,000	

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Subtotal	179,000	85,000	94,000
Deferred tax liabilities	200,000	100,000	100,000
Net deferred tax assets/liabilities	150,000	75,000	75,000

12.30 The change in net deferred income taxes is comprised of the following (this analysis is exclusive of nonadmitted assets as the Change in Nonadmitted Assets is reported separately from the Change in Net Deferred Income Taxes in the surplus section of the Annual Statement):

	Dec. 31, 20X2	Dec. 31, 20X1	Change
Adjusted gross deferred tax assets	$500,000	$200,000	$300,000
Total deferred tax liabilities	200,000	100,000	100,000
Net deferred tax assets (liabilities)	$300,000	$100,000	200,000
Tax effect of unrealized gains (losses)			(30,000)
Change in net deferred income tax			$170,000

Paragraph 25 Illustration[48(193)]:

12.31 The provision for federal and foreign income taxes incurred is different from that which would be obtained by applying the statutory Federal income tax rate to income before income taxes. The significant items causing this difference are as follows:

	Dec. 31, 20X2	Effective Tax Rate
Provision computed at statutory rate	$245,000	35.0%
Tax exempt income deduction	(102,000)	(14.6)
Dividends received deduction	(84,000)	(12.0)
Tax differentials on foreign earnings	(34,000)	(4.8)
Change in statutory valuation allowance adjustment	10,000	1.4
Nondeductible goodwill	8,000	1.1
Other	7,000	1.0
Total	$50,000	7.1%
Federal and foreign income taxes incurred	$220,000	31.4%
Change in net deferred income taxes[49(194)]	(170,000)	(24.3)
Total statutory income taxes	$50,000	7.1%

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Paragraph 26 Illustration:

12.32 The Company has net capital loss carryforwards which expire as follows: 20X5, $9,000; 20X6; $1,000.

Paragraph 27 Illustration:

12.33 The Company believes it is reasonably possible that the liability related to any federal or foreign tax loss contingencies may significantly increase within the next 12 months. However, an estimate of the reasonably possible increase cannot be made at this time.

Paragraph 28 Illustration:

12.34 The Company is included in a consolidated federal income tax return with its parent company, Alpha Corporation. The Company has a written agreement, approved by the Company's Board of Directors, which sets forth the manner in which the total combined federal income tax is allocated to each entity which is a party to the consolidation. Pursuant to this agreement, the Company has the enforceable right to recoup federal income taxes paid in prior years in the event of future net losses, which it may incur, or to recoup its net losses carried forward as an offset to future net income subject to federal income taxes.

13. Q – How are tax-planning strategies to be considered in determining adjusted gross DTAs [Paragraph 7.e.] and admitted adjusted gross DTAs [Paragraphs 11.a., 11.b.i., 14 and 15]?

Overview:

13.1 A – Paragraph 14 of SSAP No. 101 states:

> In some circumstances, there are tax-planning strategies (including elections for tax purposes) that (a) are prudent and feasible, (b) a reporting entity ordinarily might not take, but would take to prevent an operating loss or tax credit carryforward from expiring unused, and (c) would result in realization of deferred tax assets. A reporting entity shall consider tax-planning strategies in (1) determining the amount of the statutory valuation allowance adjustment necessary under paragraph 7.e. and (2) the realization of deferred tax assets when determining admission under paragraph 11…

13.2 Paragraph 248 of FAS 109 additionally states that:

> Tax-planning strategies also may shift the estimated pattern and timing of future reversals of temporary differences…. A tax-planning strategy to accelerate the reversal of deductible temporary differences in time to offset taxable income that is expected in an early future year might be the only means to realize a tax benefit for those deductible temporary differences if they otherwise would reverse and provide no tax benefit in some later future year(s).

13.3 As also provided in paragraph 14 of SSAP No. 101, if a tax-planning strategy is used to accelerate the reversal or realization of an item, any significant net-of-tax potential costs or losses

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associated with the implementation of the strategy should reduce the adjusted gross or admitted DTA.

13.4 When considering a prudent and feasible tax-planning strategy that is more likely than not to enable realization of all or part of an adjusted gross DTA or admitted DTA, paragraph 15 of SSAP No. 101 states that "paragraph 3 of this statement related to tax loss contingencies shall be applied in determining admissibility of deferred tax assets under paragraph 11 of this statement." Accordingly, a reporting entity must evaluate the likelihood, if a tax-planning strategy were implemented, of whether a tax loss contingency would be required to be recorded under paragraph 3.a. If so, the admitted tax benefit of a tax-planning strategy must be reduced by the amount of tax loss contingency so required. For example, if a tax-planning strategy provided a $100 admitted DTA, but the reporting entity estimated that a tax loss contingency reserve of $40 would be required if the strategy was implemented, the admitted DTA resulting from the tax-planning strategy would be reduced by $40. Since the admitted DTA would be net of any applicable tax loss contingencies, no separate tax loss contingencies would actually be recorded for these items.

Statutory Valuation Allowance Adjustment:

13.5 As discussed in Question 2.5, future realization of gross DTAs ultimately depends on the existence of sufficient taxable income of the appropriate character within the carryback or carryforward period available under the tax law. In determining adjusted gross DTAs, a reporting entity shall consider the four sources of taxable income that may be available under the tax law, one of which is tax-planning strategies[50(195)]. As noted in paragraph 13 of SSAP No. 101, a reporting entity is not required to consider all four sources of taxable income if one or more sources are alone sufficient to support the conclusion that the entity will realize the tax benefits of its adjusted gross DTAs (i.e., a conclusion that no statutory valuation allowance is necessary). Accordingly, tax-planning strategies need not be considered if the other sources of taxable income are sufficient to realize the benefits of reversing existing DTAs. However, the reporting entity is required to consider the impact of tax planning strategies to determine the amount of the adjustment if a conclusion is reached that a statutory valuation allowance adjustment is necessary.

Tax-Planning Strategies for Admission of DTAs:

13.6 In order for a tax-planning strategy to support admission of adjusted gross DTAs under paragraph 11, the reporting entity must demonstrate that (1) the admitted DTAs would be realized either within a period that would give rise to a carryback of tax losses under the Internal Revenue Code, not to exceed three years (for admission under paragraph 11.a.), or within the applicable period (refer to the 11.b.i. column of the applicable Realization Threshold Limitation Table in paragraph 11) and (2) it would have the ability to implement the strategy. In such circumstances an entity may recognize, as admitted assets, the related DTAs that are realizable as a result of the available tax-planning strategy in accordance with paragraphs 11.a., 11.b.i. and 11.c. of SSAP No. 101. Using tax-planning strategies in determining the admissible DTA is analogous to the use of tax-planning strategies in determining the amount of the statutory valuation allowance adjustment required under paragraph 7.e. of SSAP No. 101 and paragraph 22 of FAS 109. Although a reporting entity may use tax-planning strategies in determining the portion of its adjusted gross DTAs that are admissible, it is not required to do so.

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13.7 The requirement in paragraph 11.a. and 11.b.i. of SSAP No. 101 to consider only those DTAs that reverse or are realized within a period that would give rise to a carryback of losses under the Internal Revenue Code not to exceed three years (paragraph 11.a.) or within the applicable period following the balance sheet date (paragraph 11.b.i.) causes those DTAs which would otherwise reverse beyond such period to potentially provide no tax benefit (unless admitted under paragraph 11.c.). The potential reversal beyond the appropriate period is comparable to an expiring net operating loss, in that the deduction would not provide a tax benefit under SSAP No. 101. Thus, to the extent prudent and feasible tax-planning strategies exist to accelerate the reversal or realization of these DTAs, these strategies are comparable to those contemplated in paragraph 248 of FAS 109 above.

13.8 An example of a prudent and feasible tax-planning strategy is as follows:

13.9 Company A, a property/casualty insurance company for federal income tax purposes, has paid federal income taxes of $500,000 in each of calendar years 20X1 and 20X2. The company has an ExDTA ACL RBC percentage of 250% and therefore is required to use the one-year applicable period under paragraph 11.b.i. of SSAP No. 101. It has capital and surplus for purposes of paragraph 11.b.ii. of SSAP No. 101 of $20,000,000. Company A has an obligation to provide post-retirement health benefits to its employees. At December 31, 20X2, Company A has included a liability for $1,000,000 on its statutory-basis financial statements for post-retirement health benefits. This liability is not currently deductible for federal income tax purposes, and only $25,000 reverses within each of the next two calendar years. This is Company A's only DTA under SSAP No. 101, and there are no DTLs. Company A, absent any tax-planning strategies, would compute a DTA of $350,000 ($1,000,000 X 35%), and would admit $17,500 ($50,000 X 35%) under paragraph 11.a., and has no additional admitted DTA under paragraph 11.b.

13.10 Company A could implement a welfare benefit fund for tax purposes, and contribute assets to the fund to cover qualifying welfare benefits. The contribution, subject to limitations, would be deductible for federal income tax purposes, and would have the effect of accelerating the deduction for Company A's post-retirement health benefits. Company A has computed that $300,000 could be contributed during 20X3 to the welfare benefit fund, and to implement this strategy, it would cost $15,000 on an after-tax basis. Company A management believe that this strategy is prudent and feasible, and the Company would be able to implement this strategy if necessary. Company A would be able to admit an additional $90,000 of DTAs ($300,000 X 35%, or $105,000, less $15,000 in costs) under paragraph 11.a., with no additional admitted DTA under paragraph 11.b.

13.11 A tax-planning strategy would not be considered prudent or feasible if use of the strategy would be inconsistent with assumptions inherent in statutory or other accounting basis financial statements. For instance, a tax-planning strategy to sell securities identified as "held to maturity" for GAAP-basis financial statements at a loss would not be prudent or feasible. Additionally, if a potential tax planning strategy were to involve selling debt securities at a loss, it would not be prudent or feasible if the securities had not been identified as impaired and the loss recognized for statutory-basis financial statements. Additionally, a tax-planning strategy that could not be implemented to realize a tax benefit within the requisite period following the balance sheet date or is inconsistent with management's business plan objectives would not be prudent and/or feasible.

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