2015 NAIC QUARTERLY STATEMENT INSTRUCTIONS – FRATERNAL

MAR 2015 REVISIONS

PAGE 41: NOTES TO FINANCIAL STATEMENTS
Revision: Update list of required quarterly notes disclosures.
Reason: Disclosures added to instructions required by SAP but not included in instructions.

PAGE 42 & 43: NOTES TO FINANCIAL STATEMENTS
Revision: Add Note 1C(6) to instructions.
Reason: Required by SSAP No. 43R.

PAGE 52: NOTES TO FINANCIAL STATEMENTS
Revision: Add Note 17B(2)a and 17B(2)c to instructions.
Reason: Required by SSAP No.103.

EDITOR’S NOTE:

The above changes are highlighted within the attached instructions that follow this page.

Recent Blanks Working Group Agenda Items (Exposure Drafts) may be viewed in detail at the following web site: http://www.naic.org/committees_e_app_blanks.htm.
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NOTES TO FINANCIAL STATEMENTS

The interim financial information shall include disclosures sufficient to make the information presented not misleading. It may be presumed that the users of the interim financial information have read or have access to the annual statement for the preceding period and that the adequacy of additional disclosure needed for a fair presentation, except in regard to material contingencies, may be determined in that context. Accordingly, footnote disclosure that would substantially duplicate the disclosure contained in the most recent annual statement or audited financial statements, such as a statement of significant accounting policies and practices, details of accounts that have not changed significantly in amount or composition since the end of the most recently completed fiscal year, may be omitted but the footnote number and annotation such as “no change” should be included. However, provide disclosure for annual Note 1A, 1C(6), 5D, 5E(3)b, 5l(2), 5l(3), 5J, 11B, 12A(4), 17B(2), 17B(4)a, 17B(4)b, 17C, 20, 24E and 25 in all quarters; and all other Notes where events subsequent to the end of the most recent fiscal year have occurred that have a material impact on the reporting entity. Disclosures shall encompass, for example, significant changes since the end of the period reported on the last annual statement in such items as statutory accounting principles and practices; estimates inherent in the preparation of financial statements; status of long term contracts; capitalization including significant new borrowings or modifications of existing financial arrangements; and the reporting entity resulting from business combinations or dispositions. Notwithstanding the above, where material noninsurance contingencies exist, disclosure of such matters shall be provided even though a significant change since year-end may not have occurred. If the reporting entity has changed the accounting policies since the end of its preceding year, the changes shall be disclosed in the quarterly financial statements. Information should be reported for current year-to-date.

1. Summary of Significant Accounting Policies

Instruction:

Refer to SSAP No. 1, Disclosure of Accounting Policies, Risks & Uncertainties, and Other Disclosures, for accounting guidance regarding disclosure requirements. The major disclosure requirements are as follows:

A. This note (including a table reconciling income and surplus between the state basis and SAP basis) is to be completed, even if there are no prescribed practices or permitted practices to report. Indicate that the statement has been completed in accordance with the Accounting Practices and Procedures Manual. If a reporting entity employs accounting practices that depart from the Accounting Practices and Procedures Manual including different practices required by state law, disclose the following information about those accounting practices that affect net income, statutory surplus or risk-based capital.

Include:

• A description of the accounting practice;

• A statement that the accounting practice differs from NAIC statutory accounting practices and procedures (NAIC SAP);

• The monetary effect on net income and statutory surplus of using an accounting practice that differs from NAIC statutory accounting practices and procedures; and

• If an Insurance enterprise’s risk-based capital would have triggered a regulatory event had it not used a prescribed or permitted practice, that fact should be disclosed in the financial statements.

In addition, disclose the following information about accounting practices when NAIC statutory accounting practices and procedures do not address the accounting for the transaction:

• A description of the transaction and of the accounting practice used; and

• A statement that the NAIC statutory accounting practices and procedures do not address the accounting for the transaction.
NOTE: Amounts reported in other notes to the financial statements shall reference Note 1 if impacted by prescribed or permitted practices. The following is an example of inserting a statement within applicable notes:

Example Illustration: Note 3. Business Combinations and Goodwill

Illustration:

A. Statutory Purchase Method

1. The Company purchased 100% interest of XYZ Insurance Company on 6/30/_____. XYZ Insurance Company is licensed in 49 states and sells individual term life products exclusively.

2. The transaction was accounted for as a statutory purchase.

3. The cost was $_______, resulting in goodwill in the amount of $_______.*

4. Goodwill amortization relating to the purchase of XYZ Insurance Company was $_______ for the year ended 12/31/_____.*

* These amounts reflect prescribed or permitted practices that depart from the NAIC Accounting Practices and Procedures Manual, See Note 1, Summary of Significant Accounting Policies for additional information.

C. Disclose all accounting policies that materially affect the assets, liabilities, capital and surplus or results of operations. Include:

6. Basis at which the loan-backed securities are stated and the adjustment methodology used for each type of security (prospective or retrospective).

Illustration:

A. Accounting Practices

The financial statements of XYZ Company are presented on the basis of accounting practices prescribed or permitted by the ABC Insurance Department.

The ABC Insurance Department recognizes only statutory accounting practices prescribed or permitted by the State of ABC for determining and reporting the financial condition and results of operations of an insurance company, for determining its solvency under the ABC Insurance Law. The Accounting Practices and Procedures Manual (NAIC SAP) has been adopted as a component of prescribed or permitted practices by the state of ABC. The state has adopted certain prescribed accounting practices that differ from those found in NAIC SAP. Specifically, 1) goodwill arising from the purchase of a subsidiary, controlled or affiliated entity is written off directly to surplus in the year it originates by ABC domiciled companies. In NAIC SAP, goodwill in amounts not to exceed 10% of an insurer’s capital and surplus may be capitalized and all amounts of goodwill are amortized to unrealized gains and losses on investments over periods not to exceed 10 years, and, 2) 100% of all fixed assets are admitted by ABC domiciled companies. In NAIC SAP, fixed assets are not admitted. The Commissioner of Insurance has the right to permit other specific practices that deviate from prescribed practices.

The Company, with the explicit permission of the Commissioner of Insurance of the State of ___, records the value of its home office building at fair market value instead of at depreciated cost required by the NAIC SAP. If the home office building were carried at depreciated cost, home office property and statutory surplus would be decreased by $_______ and $______ as of December 31, 20___ (prior year end) and 20___ (current year to date), respectively. Additionally, net income would be increased by $_______ and $______ respectively, for the years then ended. Finally, if the Company had not been permitted to record the value of its home office building at fair market value, the Company’s risk-based capital would have triggered a regulatory event.
THE RECONCILIATION TABLE BELOW IS REQUIRED REGARDLESS OF WHETHER THE REPORTING ENTITY HAS ANY STATE PRESCRIBED OR PERMITTED PRACTICES.

A reconciliation of the Company’s net income and capital and surplus between NAIC SAP and practices prescribed and permitted by the State of ABC is shown below:

<table>
<thead>
<tr>
<th>NET INCOME</th>
<th>State of Domicile</th>
<th>20_____</th>
<th>20_____</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) ABC Company state basis (Page 4, Line 31, Columns 1 &amp; 3)</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
<tr>
<td>(2) State Prescribed Practices that increase/(decrease) NAIC SAP: e.g., Depreciation of fixed assets</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
<tr>
<td>(3) State Permitted Practices that increase/(decrease) NAIC SAP: e.g., Depreciation, home office property</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
<tr>
<td>(4) NAIC SAP (1-2-3=4)</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>SURPLUS</th>
<th>State of Domicile</th>
<th>20_____</th>
<th>20_____</th>
</tr>
</thead>
<tbody>
<tr>
<td>(5) ABC Company state basis (Page 3, Line 30, Columns 1 &amp; 2)</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
<tr>
<td>(6) State Prescribed Practices that increase/(decrease) NAIC SAP: e.g., Goodwill, net e.g., Fixed Assets, net</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
<tr>
<td>(7) State Permitted Practices that increase/(decrease) NAIC SAP: e.g., Home Office Property</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
<tr>
<td>(8) NAIC SAP (5-6-7=8)</td>
<td>$_________</td>
<td>$_________</td>
<td></td>
</tr>
</tbody>
</table>

NOTE: The permitted and prescribed adjustments detailed in the reconciliation illustrated above are only examples of permitted or prescribed practices that could be disclosed in the Notes to Financial Statements. Other permitted or prescribed practices not shown in the example should also be shown in the reporting entities printed and electronic notes.

C. Accounting Policy

(6) Loan-backed securities are stated at either amortized cost or the lower of amortized cost or fair value. The retrospective adjustment method is used to value all securities except for interest only securities or securities where the yield had become negative, that are valued using the prospective method.

5. Investments

Instruction:

D. Loan-Backed Securities

For loan-backed securities, disclose the following:

(1) Descriptions of sources used to determine prepayment assumptions.

(2) All securities within the scope of this statement with a recognized other-than-temporary impairment, disclosed in the aggregate, classified on the basis for the other-than-temporary impairment:

- Intent to sell.

- Inability or lack of intent to retain the investment in the security for a period of time sufficient to recover the amortized cost basis.
(3) For each security, by CUSIP, with an other-than-temporary impairment, recognized in the current reporting period by the reporting entity, as the present value of cash flows expected to be collected is less than the amortized cost basis of the securities:

- The amortized cost basis, prior to any current-period other-than-temporary impairment.
- The other-than-temporary impairment recognized in earnings as a realized loss.
- The fair value of the security.
- The amortized cost basis after the current-period other-than-temporary impairment.

(4) All impaired securities (fair value is less than cost or amortized cost) for which an other-than-temporary impairment has not been recognized in earnings as a realized loss (including securities with a recognized other-than-temporary impairment for non-interest related declines when a non-recognized interest related impairment remains):

a. The aggregate amount of unrealized losses (that is, the amount by which cost or amortized cost exceeds fair value); and
b. The aggregate related fair value of securities with unrealized losses.

The disclosures in (a) and (b) above should be segregated by those securities that have been in a continuous unrealized loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 months or longer using fair values determined in accordance with SSAP No. 27, Disclosure of Information about Financial Instruments with Off-Balance-Sheet Risk and Financial Instruments with Concentrations of Credit Risk.

(5) Additional information should be included describing the general categories of information that the investor considered in reaching the conclusion that the impairments are not other-than-temporary.

E. Repurchase Agreements and/or Securities Lending Transactions

(3) If the entity or its agent has accepted collateral that it is permitted by contract or custom to sell or repledge, disclose the following information by type of program (repurchase agreement, securities lending or dollar repurchase agreement) as of the date of each statement of financial position:

b. The fair value as of the date of each statement of financial position presented of that collateral and of the portion of that collateral that it has sold or repledged.

I. Working Capital Finance Investments

(2) Disclose the aggregate book/adjusted carrying value maturity distribution on the underlying Working Capital Finance Programs by the following categories: maturities up to 180 days and 181 days to 365 days.

(3) Disclose any events of default of working capital finance investments during the reporting period.

J. Offsetting and Netting of Assets and Liabilities

The following quantitative information shall be disclosed (separately for assets and liabilities) when derivative, repurchase and reverse repurchase, and securities borrowing and securities lending assets and liabilities are offset and reported net in accordance with a valid right to offset per SSAP No. 64, Offsetting and Netting of Assets and Liabilities:

- The gross amounts of recognized assets and recognized liabilities;
- The amounts offset in accordance with a valid right to offset per SSAP No. 64, Offsetting and Netting of Assets and Liabilities; and
- The net amounts presented in the statement of financial positions.

Assets and liabilities that have a valid right to offset, but are not netted as they are prohibited under SSAP No. 64, Offsetting and Netting of Assets and Liabilities, are not required to be captured in the disclosures.
12. Retirement Plans, Deferred Compensation, Postemployment Benefits and Compensated Absences and Other Postretirement Benefit Plans

The disclosures required for this Note shall be aggregated for all of a reporting entity’s defined benefit pension plans and for all of a reporting entity’s other defined benefit postretirement plans unless disaggregating in groups is considered to provide useful information or is otherwise required by SSAP No. 92, Postretirement Benefits Other Than Pensions, A Replacement of SSAP No. 14 or SSAP No. 102, Accounting for Pensions, A Replacement of SSAP No. 89. Disclosures shall be as of the date of each statement of financial position presented. Disclosures about pension plans with assets in excess of the accumulated benefit obligation generally may be aggregated with disclosures about pension plans with accumulated benefit obligations in excess of assets. The same aggregation is permitted for other postretirement benefit plans. If aggregate disclosures are presented, a reporting entity shall disclose:

- The aggregate benefit obligation and aggregate fair value of plan assets for plans with benefit obligations in excess of plan assets as of the measurement date of each statement of financial position presented.
- The aggregate pension accumulated benefit obligation and aggregate fair value of plan assets for pension plans with accumulated benefit obligations in excess of plan assets.

Refer to SSAP No. 11, Postemployment Benefits and Compensated Absences; SSAP No. 92, Postretirement Benefits Other Than Pensions, A Replacement of SSAP No. 14; and SSAP No. 102, Accounting for Pensions, A Replacement of SSAP No. 89, for additional guidance.

Instruction:

A. Defined Benefit Plan

(4) The amount of net periodic benefit cost recognized, showing separately:

a. Service cost
b. Interest cost
c. Expected return on plan assets for the period
d. Transition asset or obligation
e. Gains and losses
f. Prior service cost or credit
g. Gain or loss recognized due to a settlement or curtailment
h. Total net periodic benefit cost

Illustration:

A. Defined Benefit Plan

(4) Components of net periodic benefit cost

<table>
<thead>
<tr>
<th></th>
<th>Pension Benefits</th>
<th>Postretirement Benefits</th>
<th>Postemployment &amp; Compensated Absence Benefits</th>
</tr>
</thead>
<tbody>
<tr>
<td>20_</td>
<td>20_</td>
<td>20_</td>
<td>20_</td>
</tr>
<tr>
<td>a. Service cost</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>b. Interest cost</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>c. Expected return on plan assets</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>d. Transition asset or obligation</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>e. Gains and losses</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>f. Prior service cost or credit</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>g. Gain or loss recognized due to a settlement or curtailment</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
<tr>
<td>h. Total net periodic benefit cost</td>
<td>$______</td>
<td>$______</td>
<td>$______</td>
</tr>
</tbody>
</table>
B. Transfer and Servicing of Financial Assets

For transactions reported in accordance with SSAP No. 103, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, a reporting entity shall disclose the following:

(2) For all servicing assets and servicing liabilities:

a. A description of the risks inherent in servicing assets and servicing liabilities and, if applicable, the instruments used to mitigate the income statement effect of changes in fair value to the servicing assets and servicing liabilities. (Disclosure of quantitative information about the instruments used to manage the risks inherent in servicing assets and servicing liabilities is encouraged but not required.)

b. The amount of contractually specified servicing fees, late fees and ancillary fees earned for each period for which results of operations are presented, including a description of where each amount is reported in the statement of income.

c. Quantitative and qualitative information about the assumptions used to estimate the fair value (for example, discount rates, anticipated credit losses, and prepayment speeds). An entity that provides quantitative information about the instruments used to manage the risks inherent in the servicing assets and servicing liabilities, as encouraged by SSAP No. 103, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, also is encouraged, but not required to disclose the quantitative and qualitative information about the assumptions used to estimate the fair value of those instruments.

(4) For securitizations, asset-backed financing arrangements and similar transfers accounted for as sales when the transferor has continuing involvement (as defined in the glossary of the Accounting Practices and Procedures Manual) with the transferred financial assets:

a. For each income statement presented:

1. The characteristics of the transfer (including a description of the transferor’s continuing involvement with the transferred financial assets, the nature and initial fair value of the assets obtained as proceeds and the liabilities incurred in the transfer, and the gain or loss from the sale of transferred financial assets. For initial fair value measurements of assets obtained and liabilities incurred in the transfer, the following information:

   (a) The level within the fair value hierarchy in which the fair value measurements in their entirety fall, segregating fair value measurements using quoted prices in active markets for identical assets or liabilities (Level 1), significant other observable inputs (Level 2) and significant unobservable inputs (Level 3).

   (b) The key inputs and assumptions used in measuring the fair value of assets obtained and liabilities incurred as a result of the sale that relate to the transferor’s continuing involvement (including, at a minimum, but not limited to, and if applicable, quantitative information about discount rates; expected prepayments, including the expected weighted-average life of prepayable financial assets; and anticipated credit losses, including expected static pool losses).

      • If an entity has aggregated multiple transfers during a period, it may disclose the range of assumptions.

      • The weighted-average life of prepayable assets in periods (for example, months or years) can be calculated by multiplying the principal collections expected in each future period by the number of periods until that future period, summing those products, and dividing the sum by the initial principal balance.

      • Expected static pool losses can be calculated by summing the actual and projected future credit losses and dividing the sum by the original balance of the pool of assets.

2. Cash flows between a transferor and transferees, including proceeds from new transfers, proceeds from collections reinvested in revolving-period transfers, purchases of previously transferred financial assets, servicing fees and cash flows received from a transferor’s beneficial interests.