To: Statutory Accounting Principles (E) Working Group
From: Julie Gann (NAIC Staff)
Re: Discussion – Inclusion of Security Definition in SSAP No. 26
Date: December 17, 2014 - (Exposed for Comment on March 28, 2015)

This memorandum details proposed revisions to include a definition to the term “security” within the definition of a bond in SSAP No. 26—Bonds, Excluding Loan-Backed and Structured Securities.

Proposal: Incorporate the GAAP definition of a security, as it is used in FASB Codification Topic 320: Investments – Debt and Equity Securities, and Topic 860: Transfers and Servicing:

Security: A share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:

a. It is either represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.

b. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.

c. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

This definition is already included in SSAP No. 37—Mortgage Loans, paragraph 2.

2. A mortgage loan is defined as a debt obligation that is not a security, which is secured by a mortgage on real estate. (A security is a share, participation, or other interest in property or in an enterprise of the issuer or an obligation of the issuer that (a) either is represented by an instrument issued in bearer or registered form, or if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer, (b) is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment, and (c) either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations).

Rationale – Staff does not see a regulatory reason to define “security” differently between GAAP & SAP.

Impact: By incorporating the definition of a security in SSAP No. 26, it will be clear that some investments within scope of SSAP No. 26 do not meet the definition of a bond. Although the inclusion of these investments will be subsequently considered under the investment project, for this discussion topic, it is proposed that the guidance in SSAP No. 26 be divided between those items that meet the explicit definition of a bond, and investments that have been previously decided to be reported as bonds. Consideration should subsequently occur on whether the GAAP security definition should be included in the AP&P Manual master glossary for all references within the Manual. If this definition is supported for SSAP No. 26, staff will identify all of the SSAPs and references that would be impacted and present this info for subsequent Working Group discussion.
Proposed Revisions to SSAP No. 26 – Include Security Definition

Bonds, Excluding Loan-Backed and Structured Securities

SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for bonds and fixed-income investments specifically identified to be within the scope of this statement.

2. This statement excludes:
   a. Loan-backed and structured securities. These investments are addressed in SSAP No. 43R—Loan-Backed and Structured Securities.
   b. Bonds that meet the definition in paragraph 3, but have a maturity date of one year or less from the date of acquisition. These investments are addressed in SSAP No. 2—Cash, Drafts and Short-Term Investments.
   c. Mortgage loans and other real estate lending activities made in the ordinary course of business. These investments are addressed in SSAP No. 37—Mortgage Loans and SSAP No. 39—Reverse Mortgages.

SUMMARY CONCLUSION

1-3. Bonds shall be defined as any securities representing a creditor relationship, whereby there is a fixed schedule for one or more future payments. This definition includes:
   a. U.S. Treasury securities,
   b. U.S. government agency securities,
   c. Municipal securities, and
   d. Corporate bonds.
   d. Convertible debt bonds, including mandatory convertible debt bonds as defined in paragraph 9.

NOTE: Other items currently included in SSAP No. 26 will be subsequently discussed. The intent of this memo is simply to consider including the definition for a “security”.

1 This SSAP adopts the GAAP definition of a security as it is used in FASB Codification Topic 320 and 860: Security: A share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:
   a. It is either represented by an instrument issued in bearer or registered form or, if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.
   b. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.
   c. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.