PLANNING FOR PRINCIPLES-BASED BOND DEFINITION TRANSITION

A guide to planning for the principles-based bond definition transition

The Principles-Based Bond Definition provides a conceptual framework for better classifying bonds, structured securities, and asset-backed securities for accounting, reporting and risk. It represents a significant, multifaceted change for insurers and brings with it a need for investors to deeply understand the sources and priority of cash flows that will repay the obligation for fixed income and asset-backed securities.

Beginning January 1, 2025, changes will impact the front, middle and back office all the way through to the Statutory Annual Statement. This will affect insurers in varying ways, depending the composition of the investment portfolio and the degree to which they outsource investment accounting and operations. This guide helps insurers prepare for a smooth transition by outlining concerns and questions insurance investment accounting leaders should be considering as we get closer to 2025.

Four key areas will see big changes next year

1

RE-CATEGORIZATION

Reporting categories for Long-Term Fixed Income investments are changing and becoming much more granular. This requires deep understanding of the new guidance and the underlying structures of the investments to ensure investments are categorized correctly.

2

NEW DATA POINTS

For year-end 2025, there are both new and revised supplementary investment information for the Schedule D Part 1 schedules. These provide additional attributes for regulators on the nature of the investments. Some of the data points are not part of standard data feeds from industry providers.

3

REPORTING CHANGES

The new categories will go into effect for Q1 2025 reporting and for year end, the Schedule D Part splits into two sections for Long-Term Bonds and Asset-Backed Securities with numerous related changes. The new guidance also requires certain bonds to be reported on Schedule BA Part 1 (Other Invested Assets).

4

RISK-BASED CAPITAL

Risk-Based Capital (RBC) charges are aligned around the Reporting Schedules, Categories and Ratings of securities. Based on the nature of the portfolio, the new guidance may cause increases to the RBC charges and should be considered for investment decisions going forward.

Key questions insurers should ask

The ways investment accounting, data services, investment management and financial reporting are structured for an organization will impact the questions you need to ask. If a third-party provider does the work, there are different conversations that need to take place versus when the processes are managed within an organization.

The matrix below lays out important questions that insurers with both outsourced and in-house service models can address. Answering these questions will help identify aspects of their systems and processes that may need attention before Q1 2025.

Key Area	Outsourced Service Model	In-House Service Model
Re-Categorization	What type of training is happening for the service team and is there training available for clients? How will the process work for identifying categories? How will the review process work to identify changes or overrides for category assignments? Are there additional fees for the categorization project?	How do we train our internal teams about the new guidance? Does the software package provide any automation or tools to help suggest and automate the transition? How will the process work for identifying categories? How will current workflows and automation change? When will software changes be available to capture the new categories? Will the software provide the ability to parallel the 2024 reporting with a pro forma view of 2025 reporting?
New Data Points	What type of training is happening for the service team and is there training available for clients? How will the process work for identifying categories? How will the review process work to identify changes or overrides for category assignments? Are there additional fees for the categorization project?	When will the data capture (both interactive and upload) be made available in the system? Are there any version restrictions for obtaining the necessary updates? Will information be shared about potential or recommended sources for new data elements? Are there any new automation tools or processes associated with the new data points?
Reporting Changes	Will there be a recommended process and automation to support the movement of assets between schedules per the NAIC guidance? When will the Q1 2025 Quarterly Reporting changes be available? When will the Q4 2025 Annual Reporting changes be available? Will there be an ability to compare the year-end 2024 filings with the changes for 2025?	
Risk-Based Capital	Will there be any reporting or tools that can help quantify the impact to RBC charges to assess the capital charges with our year-end filing data?	

It is all in the timing

With the first reporting changes going into effect in 2025, it may seem to insurers like there is plenty of time to prepare However, the time for action is now.

It is reasonable that companies may be hyper-focused on the impacts to RBC charges. There is a cautionary tale embedded here. It is all too easy to think that minimal RBC charges reduce the overall effort required for the transition to the Principles Based Bond Definition. In reality, the operational, workflow and reporting changes should be given equal weight in the review and planning processes, to ensure a smooth transition. Failing to do the planning and testing before year-end 2024 could leave you scrambling to meet or missing first quarter filing dates and burning out the accounting and reporting staff in the process.

To hit the ground running on January 1, organizations should address each of the questions provided in the matrix on the previous page to ensure there are no gaps in your plan. They should also:

- Look out for communications from the NAIC.
- Take advantage of any materials, webinars, conferences, or client team meetings that discuss the upcoming changes.
- Create an action plan that includes educating your teams, identifying data sources, and testing and adopting any system changes needed.

And remember – SS&C has experts who are available to answer questions and work through challenges that come with the Principles-based Bond Definition Transition. You can reach us here. We'd be happy to help.

Failing to plan, is planning to fail.

—Benjamin Franklin

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