

Statutory Issue Paper No. 12

Accounting for Drafts Issued and Outstanding

STATUS

Finalized March 16, 1998

Original SSAP; SSAP No. 2; Current Authoritative Guidance: SSAP No. 2R

Type of Issue:

Common Area

SUMMARY OF ISSUE

1. Current statutory accounting, as documented in the Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies, provides guidance on the accounting for drafts but does not provide a definition of a draft. This issue paper will establish a definition for “draft” and will codify statutory accounting relating to drafts.

SUMMARY CONCLUSION

2. For purposes of statutory accounting, a “draft” is defined as an order to pay a sum certain in money, which is signed by the drawer (e.g., the insurance company or its agent), and payable to order or bearer (policyholder) by the drawee (bank) only upon approval by the insurance company once the draft has been presented to the drawee.

3. A reporting entity that utilizes instruments that meet the above definition of drafts shall elect one of the following accounting methods:

a. **Draft Issued Method** - When a draft is issued, an increase in paid losses and a related decrease in loss reserves is recorded. Drafts that have not been presented for payment and remain outstanding at the balance sheet date are reflected as a liability.

b. **Draft Honored Method** - An increase in paid losses and a related decrease in loss reserves is recorded when the draft is cashed and presented by the bank to the reporting entity for reimbursement. Consequently, under a draft honored method there is no liability for outstanding drafts.

The method elected by a reporting entity to account for drafts issued and outstanding shall remain consistent from year to year. Procedures for changes in the accounting method shall be governed by *Issue Paper No. 3—Accounting Changes*.

DISCUSSION

4. Statutory accounting does not address the characteristics of a draft, however, Chapter 13, *Other*

