

Statutory Issue Paper No. 155

Classification of Money Market Mutual Funds as Cash Equivalents

STATUS

Finalized December 10, 2016

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

**Type of Issue:
Common Area**

SUMMARY OF ISSUE

1.

Cash, Cash Equivalents, Drafts and Short-Term Investments**SCOPE OF STATEMENT**

1. This statement establishes statutory accounting principles and related reporting for cash, cash equivalents, drafts and short-term investments.

SUMMARY CONCLUSION**Cash**

2. Cash constitutes a medium of exchange that a bank or other similar financial institution will accept for deposit and allow an immediate credit to the depositor's account.

3. Cash meets the definition of an asset as defined in SSAP No. 4—Assets and Nonadmitted Assets (SSAP No. 4), and is an admitted asset to the extent it conforms to the requirements of this statement.

4. If a reporting entity has multiple cash accounts, the net amount of all accounts shall be reported jointly. Cash accounts with positive balances shall not be reported separately from cash accounts with negative balances. If in the aggregate, the reporting entity has a net negative cash balance, it shall be reported as a negative asset and shall not be recorded as a liability.

3.5. Also classified as cash for financial statement purposes, although not falling within the definition of cash, are savings accounts and certificates of deposit in banks or other similar

When the draft is presented to the drawee (i.e., the bank), it is paid only upon approval by the reporting entity.

9. _____ Drafts and checks have different legal characteristics. A check is payable on demand, whereas a draft must be approved for payment by the reporting entity before it is honored by the bank. Because of these different characteristics, a draft meets the definition of a liability as defined by *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets*. Outstanding checks are accounted for as a reduction of cash.

5.10. _____ A reporting entity that utilizes instruments meeting the 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 presented by the bank to the reporting entity for approval and reimbursement. Consequently, under a draft honored method there is no liability for outstanding drafts.

~~44.16.~~ Refer to the Preamble for further discussion regarding disclosure requirements. The disclosures in paragraph ~~43~~15.b. shall be included in the annual audited statutory financial reports only.

Effective Date and Transition

~~42.17.~~ This statement is effective for years beginning January 1, 2001. 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. Guidance in paragraph ~~3-6~~ related to terms reset at predefined dates was previously included within *INT 08-10: Contractual Terms of Investments and Investor Intent* and was effective for periods beginning December 5, 2008. This substantively revised statement, as detailed in Issue Paper No. 155, regarding treatment of MMMF as cash equivalents, is effective on a prospective basis beginning December 31, 2017.

REFERENCES

Other

Purposes and Procedures Manual of the NAIC Investment Analysis Office

Relevant Issue Papers

Issue Paper No. 2—Definition of Cash

Issue Paper No. 12—Accounting for Drafts Issued and Outstanding

Issue Paper No. 28—Short-Term Investments

Issue Paper No. 155—Classification of Money Market Mutual Funds as Cash Equivalents

Historical Discussion

5. During 2002-2003, at the request of an industry sponsored Form A, the Working Group previously considered an agenda item (Ref #2002-14) on whether to classify MMMF as cash equivalents.

6. In May 2002, an industry sponsored Form A was submitted to the Working Group, requesting that consideration be given to classifying MMMF as cash equivalents. The request, while noting that MMMF do not have a stated maturity date, stated that underlying characteristics of MMMF are similar to a checking or savings account, which are “on-demand” accounts and reported on Schedule E. Further, the proposal highlighted several benefits to the insura

8. At the 2003 Fall National Meeting, NAIC staff presented a memorandum to the Working Group, which questioned the extent of benefits to be gained by changing the classification and other claims made in the sponsor's Form A, including whether U.S. GAAP explicitly expresses that MMMF are cash equivalents and inconsistencies that would still exist between U.S. GAAP and SAP even if MMMF were classified as cash equivalents for statutory accounting. The memorandum highlighted that making this classification change would make GAAP and SAP more consistent in some instances for Exempt and Class One MMMF, but insurers would still be reporting the remaining MMMF in Schedule D, Part 2, section 2, along with common stocks. (*Staff Note: This inconsistency is no longer relevant due to the Working Group's June 2016 actions to have all MMMF classified as short-term investments on Schedule DA-see below*). At this meeting, the Working Group exposed the industry sponsor's Form A, with the edits recommended by the Invested Assets (E) Working Group, and the NAIC staff memorandum discussed above.

9. At the 2003 Winter National Meeting, the Working Group held a public hearing of comments on the exposed Form A and NAIC staff memorandum. After consideration of the comments received and the concerns identified in the NAIC staff memorandum, the Working Group proceeded with rejecting/disposing of the agenda item (Ref #2002-14) without revisions to statutory accounting.

10. On June 9, 2016, the Working Group adopted revisions to SSAP No. 2, SSAP No. 26, SSAP No. 30, and SSAP No. 32—*Preferred Stock* (Ref #2016-05) to remove the reference to "Class 1 Money Market Mutual Funds," as a result of changes in U.S. Securities and Exchange Commission (SEC) money market mutual fund regulations, and corresponding revisions to the *Purpose and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual). The adopted revisions clarify that MMMF are considered short-term investments and should be reported on Schedule DA. The Working Group sent a referral to the Blanks (E) Working Group requesting that the existing reporting line previously used for "Class 1 Money Market Mutual Funds" on Schedule DA be retained, but renamed to "Other Money Market Mutual Funds." The Blanks (E) Working Group adopted this change on its June 17, 2016 conference call. As a result of this change, all money market mutual funds were to be reported as short-term investments on Schedule DA as either "Exempt Money Market Mutual Funds" or "Other Money Market Mutual Funds."

11. On the June 9 conference call, in response to comments received, the Working Group directed NAIC staff to develop a new agenda item (Ref #2016-19), with the assistance of interested parties, for subsequent consideration during the 2016 Summer National Meeting on whether MMMF should be accounted and reported as cash equivalents for statutory accounting.

12. At the 2016 Summer National Meeting, the Working Group exposed revisions to SSAP No. 2 to reclassify money market mutual funds from short-term investments to cash equivalents, with prospective application as of January 1, 2018. In addition to the agenda item, staff developed a proposed substantively revised SSAP No. 2R and related issue paper for concurrent exposure. Further, the Working Group sent notice to the Blanks (E) Working Group and Capital Adequacy (E) Task Force regarding the discussion about potential reclassification of MMMF as cash equivalents.

13. As detailed in paragraphs 14-25, this issue paper provides documentation of key topics discussed by the Working Group in their consideration and ultimate adoption of substantive revisions to SSAP No. 2 to reclassify MMMF from short-term investments to cash equivalents.

Classification and Regulation of MMMF by U.S. GAAP and the SEC

14. In 2014, the SEC adopted amendments to Rule 2a-7 under the Investment Company Act of 1940, as amended, which governs the operation of U.S. money market funds. As stated in their release of these amendments³, "the Commission's position continues to be that, under normal circumstances, an investment in a money market fund that has the ability to impose a fee or gate under rule 2a-7(c)(2)

³ <https://www.sec.gov/rules/final/2014/33-9616.pdf>

qualifies as a “cash equivalent” for purposes of U.S. GAAP.” Per the SEC⁴, a money market fund is a type of mutual fund that is required by law to invest in low-risk securities and have relatively low risks compared to other mutual funds.

15. As stated in their comments letters, BlackRock (dated May 11, 2016) and interested parties (dated May 20, 2016) support revising the guidance in SSAP No. 2 to reclassify MMMF from short-term investments to cash equivalents. These comment letters emphasize that the AICPA and each of the Big Four accounting firms agree with the SEC ruling that U.S. GAAP would not preclude a money market fund, including those with a floating net asset value (NAV) or the ability to impose fees and gates, from being classified as a cash equivalent. Current U.S. GAAP, as reflected in ASC 305-10-20, defines cash equivalents as “short-term, highly liquid investments that are readily convertible to known amounts of cash and that are so near their maturity that they present insignificant risk of changes in value because of changes in interest rates.” Further, ASC 305-10-20 specifically identifies an investment in a money market fund as an example of a cash equivalent.

16. Although they do not have a stated maturity date, MMMF are considered cash equivalents under U.S. GAAP, primarily invest in assets that would be classified as cash equivalents if held directly by the insurer and are commonly used in sweep accounts. Exhibit A of this issue paper includes an analysis of the Top 10 (largest) taxable institutional money market funds (based on asset size), which includes a breakout of how each MMMF is allocated across asset classes and the weighted average maturity (days).

17. Per Rule 2a-7, MMMF portfolios are not allowed to include any security that has a remaining maturity of over 397 calendar days and must maintain a dollar-weighted average portfolio maturity that does not exceed 60 days. As shown in Exhibit A, the weighted average portfolio maturity for the Top 10 MMMF is 30 days.

18. Per Rule 2a-7, MMMF portfolios shall limit investments to US denominated securities that

21. Upon re-classification of MMMF as cash equivalents, as detailed in Exhibit B, all MMMF previously classified as “Other MMMF” would incur no change in their RBC charge, as Schedule E applies the same RBC factor that is used on Schedule DA for “Other MMMF.” However, the change to cash equivalents would cause an RBC charge increase (0% to .3% for P/C and 0% to .4% for Life) for MMMF classified on the U.S. Direct Obligations / Full Faith and Credit Exempt List, as they have previously received no RBC charge when reported on Schedule DA.

Annual Statement Reporting Considerations

22. Per the revisions adopted by the Working Group and the Blanks (E) Working Group during June 2016, all MMMF were classified as short-term investments and reported as follows:

- a. Assets Page: Line 5—Cash, Cash Equivalents and Short-Term Investments
- b. Schedule DA: Exempt Money Market Mutual Funds and Other Money Market Mutual Funds

therefore the conclusions reached in this issue paper should not be applied until the corresponding SSAP has been adopted by the NAIC Executive (EX) and Plenary of the NAIC. It is expected that the SSAP will contain an effective date of reporting periods beginning December 31, 2017. The revisions outlined in this issue paper shall be applied on a prospective basis.

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

Statutory Accounting

SSAP No. 2R—Cash, Cash Equivalents, Drafts and Short-Term Investments

Generally Accepted Accounting Principles

ASC 305-10-20, Cash Equivalents-Overall-Glossary

Exhibit A

Analysis of Selected Money Market Mutual Funds

Fund Name ¹	Date of Information ²	Total Net Assets (\$mils)	Asset Allocation						Weighted Average Maturity
			Commercial Paper	Certificates of Deposit	Time Deposits	Repurchase Agreements	US Govt & Agencies	Other ³	
BlackRock Liquidity: TempFund Inst	5/31/2016	\$66,200.9	22.3%	35.7%	34.1%	6.3%	1.4%	0.2%	27
JPMorgan Prime Money Mkt Fund/Capital	6/30/2016	\$55,873.4	19.3%	44.1%	22.0%	11.1%	1.8%	1.7%	23
Goldman Sachs FS Govt Fund/Inst	5/31/2016	\$52,343.7	0.0%	0.0%	0.0%	57.8%	42.1%	0.1%	33
Fidelity Inv Prime MMF/Inst	5/31/2016	\$51,345.4	7.7%	39.7%	30.4%	18.1%	4.1%	0.0%	23
Goldman Sachs FS Treasury/Inst	5/31/2016	\$48,927.8	0.0%	0.0%	0.0%	0.0%	100.0%	0.0%	38
State Street Inst Liquid Reserve/Premier	6/30/2016	\$41,294.7	33.7%	41.5%	0.0%	15.1%	4.8%	4.9%	28
JPMorgan US Govt MMF/Capital	6/30/2016	\$37,082.8	0.0%	0.0%	0.0%	43.8%	56.2%	0.0%	33
Blackrock Liquidity: T-Fund Inst	5/31/2016	\$36,198.7	0.0%	0.0%	0.0%	48.5%	51.5%	0.0%	40
Morgan Stanley ILF/Govt/Inst	6/30/2016	\$35,276.7	0.0%	0.0%	0.0%	0.0%	100.0%	0.0%	32
Goldman Sachs FS MMF/Inst	5/31/2016	\$26,989.0	21.5%	30.7%	21.5%	20.3%	0.6%	5.4%	25
Average			10.4%	19.2%	10.8%	22.1%	36.3%	1.2%	30

¹ Top 10 (largest) taxable institutional money market funds based on asset size per iMoneyNet's Money Fund website dated July 5, 2016.

² Data obtained from publically available Fund Fact Sheet or information on file with the SEC.

³ Includes other eligible Rule 2a-7 investments.

Exhibit B

Risk-Based Capital Considerations

Per the revisions adopted by the Statutory Accounting Principles (E) Working Group and Blanks (E) Working Group in June 2016, MMMF currently receive the following RBC charges:

