Interpretation of the Emerging Accounting Issues (E) Working Group

INT 08-10: Contractual Terms of Investments and Investor Intent

ISSUE NULLIFIED BY SSAP NO. 2

INT 08-10 Dates Discussed

September 22, 2008; December 5, 2008

INT 08-10 References

SSAP No. 2—Cash, Drafts and Short-Term Investments (SSAP No. 2)

INT 08-10 Issue

1. Investments in debt instruments and other instrument types with original maturities greater than one year may include terms that periodically reset or other features that investors may view as allowing the instrument to be considered a short-term instrument or cash equivalent. An example of such a security would be the auction-rate security that has a long-term maturity and an interest rate that is regularly reset through a dutch auction. At predefined intervals, the interest rate is set by the broker/dealer based on submitted bids from buyers and sellers of the bonds. Typically, auctions are held every 7, 28, or 35 days, with interest being paid at the end of each auction.

2. Numerous inquiries have been received related to the ability to account for such investments with contractual maturity dates in excess of one year at the date of acquisition as short-term investments or as cash equivalents.

3. Guidance for cash equivalents and short-term investments is currently included within *SSAP No. 2—Cash, Draft, and Short-term Investments*:

> 3. Also classified as cash for financial statement purposes, although not falling within the above definition of cash, are savings accounts and certificates of deposit in banks or other similar financial institutions with maturity dates within one year or less from the acquisition date, and cash equivalents. Cash equivalents are short-term, highly liquid investments that are both (a) readily convertible to known amounts of cash, and (b) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Only investments with original maturities[1] of three months or less qualify under this definition.
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> 10. All investments with remaining maturities (or repurchase dates under repurchase agreements) of one year or less at the time of acquisition (excluding those investments classified as cash equivalents as defined in paragraph 3) shall be considered short-term investments. Short-term investments include, but are not limited to, bonds, commercial paper, money market instruments, repurchase agreements, and collateral and mortgage loans which meet the above criteria. Short-term investments shall not include certificates of deposit.
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> 11. All short-term investments shall be accounted for in the same manner as similar long-term investments. Investments in money market funds shall be reported in

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1 Original maturity means original maturity to the entity holding the investment. For example, both a three-month U.S. Treasury bill and a three-year Treasury note purchased three months from maturity qualify as cash equivalents. However, a Treasury note purchased three years ago does not become a cash equivalent when its remaining maturity is three months.

accordance with the guidance in the *Purposes and Procedures Manual of the NAIC Securities Valuation Office*.

12. Short-term investments meet the definition of assets as defined in SSAP No. 4 and are admitted assets to the extent they conform to the requirements of this statement.

4. The accounting issue is whether securities should be classified as 'short-term investments' or as 'cash equivalents' if they have the ability, as described above, to reset certain terms within a period that differs from the original terms at acquisition. Furthermore, the issue includes whether a 'short-term investment' or 'cash equivalent' accounting treatment is appropriate for other securities with features that an investor believes results in a shorter term than the related contractual maturity.

INT 08-10 Discussion

5. The Working Group reached a consensus that investments in securities with terms that are reset at predefined dates or have other features an investor may believe results in a different term than the related contractual maturity shall be accounted for based on the contractual maturity at the date of acquisition, except where other specific rules within the statutory accounting framework currently exist.

INT 08-10 Status

6. No further discussion planned.