LDTI Disclosures Are Here. Are You Ready?

February 17, 2023

In August 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update (ASU) 2018-12, which is also known as Targeted Improvements to the Accounting for Long-Duration Contracts ("LDTI"). For insurance companies, the accounting changes necessary to comply with ASU 2018-12 are expected to have significant impacts on U.S. GAAP financial statements. For example, guaranteed benefits associated with variable annuity and certain fixed annuity business (*i.e.*, living and death benefits) will be presented on the balance sheet as a "market risk benefit" and will be measured at fair value, resulting in greater market sensitivity of earnings for many life and retirement companies. Issuers of life insurance and long-term disability insurance will also be significantly affected by the requirement to update their discount rate assumption quarterly, based on an upper-medium grade fixed-income instrument, and recognize changes in other comprehensive income.

LDTI became effective as of January 1, 2023, with certain changes requiring retrospective application back to January 1, 2021, which is known as the transition date. As a result, for affected calendar-year reporting insurance companies, financial statements for the first quarter of 2023 (including the prior-year period) will be the first financial statements that reflect the impact of LDTI. An affected company's retrospectively revised financial statements as of and for the years ended December 31, 2022 and 2021 will also need to be included, at the latest, in the Form 10-K for the year ended December 31, 2023. However, for companies that require access to the capital markets in the period between filing their first quarter 2023 Form 10-Q and their 2023 Form 10-K, it may be necessary to file recast financial statements as of and for the years ended December 31, 2022 and 2021 sooner. For example, if a company plans to file a registration statement (*e.g.*, a Form S-1 or a new Form S-3) during this period, the company would be required to file the recast financial statements before the registration statement may be declared or become effective. While a company with an already effective Form S-3 may continue to use that Form S-3 without filing recast financial statements if it is comfortable that the change in accounting principle does not constitute a "fundamental change" (under the SEC's rules), it may nonetheless be necessary to provide selected recast financial information if the effects of LDTI on the company's financial statements are material.

As a result, many insurance companies are considering filing recast financial statements for the years ended December 31, 2022 and 2021 to reflect the impact of LDTI prior to the Form 10-K for the year ended December 31, 2023. For an already public company, these financial statements should be filed on a Form 8-K, together with retrospectively revised MD&A. The SEC made clear in its recently updated Financial Reporting Manual that the financial statements as of and for the year ended December 31, 2020 do not need to be recast, even if those financial statements are required to be included in a registration statement.

Companies should consider whether there are investor relations, Regulation FD or other reasons to furnish or file the recast financial statements sooner than required, and provide recast financial supplements or investor presentations, including to allow for comparison with peers, so that investors and analysts can assess the impact of LDTI on the company's historical financial statements.

We would be happy to discuss any of the foregoing disclosure considerations in greater detail.

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