NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Draft date: 11/2/26

Virtual Meeting

FINANCIAL ANALYSIS SOLVENCY TOOLS (E) WORKING GROUP
Monday, November 9, 2026
1:00 – 2:00 p.m. ET / 12:00 – 1:00 p.m. CT / 11:00 a.m. – 12:00 p.m. MT / 10:00 – 11:00 a.m. PT

ROLL CALL

Danielle Smith, Chair	Missouri	Kristin Hynes	Michigan
Amy Garcia, Vice Chair	Texas	Paul Lupo	New Jersey
Richard Russell/Todrick Burks	Alabama	Victor Agbu	New York
Dave Lathrop	Arizona	Tracy Snow/Mark Boston	Ohio
Michelle Lo	California	Ryan Rowe	Oklahoma
Jack Broccoli	Connecticut	Ryan Keeling	Oregon
N. Kevin Brown	District of Columbia	Liz Ammerman	Rhode Island
Carolyn Morgan/Shalice Rivers	Florida	Samantha Watkins	South Dakota
Amanda Denton	Indiana	Greg Chew	Virginia
Gregory Ricci	Maryland	Kristin Forsberg	Wisconsin

NAIC Committee Support: Rodney Good/Ralph Villegas/John Murray

AGENDA

1. Receive Comments and Consider Adoption of Proposed Revisions to the Financial Analysis Handbook—*Danielle Smith (MO)*
   a. Comment Letters — Attachment A
   b. Handbook Exposure with Edits — Attachment B

2. Discuss Any Other Matters Brought Before the Working Group —*Danielle Smith (MO)*

3. Adjournment

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Attachment A

November 2, 2026

Ms. Danielle Smith, Chair
Financial Analysis Solvency Tools (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1000
Kansas City, MO 64106-2197

Re: Second Exposure of Proposed Revisions to the Financial Analysis Handbook

Submitted Electronically

Dear Chair Smith:

On behalf of the American Council of Life Insurers (ACLI), we appreciate the Financial Analysis Solvency Tools (E) Working Group's (FASTWG) consideration of the comments we submitted on the first exposure (July 30, 2026) of the proposed revisions to the *Financial Analysis Handbook*. We also appreciate the additional time provided to review this second exposure (October 19, 2026).

The revised exposure reflects meaningful consideration of stakeholder feedback. In particular, we appreciate the revisions that provide greater context regarding private assets, recognize distinctions among different types of private investments, and emphasize the importance of materiality and an insurer's broader risk profile. We also appreciate revisions that frame certain detailed information requests and transaction terms as examples rather than generally applicable expectations. We respectfully offer the following additional comments.

Unfunded Commitments

ACLI appreciates the addition of procedures for evaluating unfunded commitments and agrees that these commitments should be considered in the context of an insurer's liquidity planning, cash-flow forecasting, and overall asset-liability management.

The second exposure includes a procedure to review Schedule BA, Part 1, Column 19, "Commitment for Additional Investment," as a percentage of Policyholders' Surplus. Consistent with the approach taken for other ratios in the revised Handbook, ACLI recommends adding a separate ratio based on total assets.

As noted in our comments on the first exposure, ratios using capital and surplus as the denominator may produce misleading outliers in certain circumstances, including where the denominator does not reflect capital supporting business that has been reinsured but the assets supporting that business remain on

The American Council of Life Insurers (ACLI) is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI's member companies are dedicated to protecting consumers' financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI's 275 member companies represent 94 percent of industry assets in the United States.

the cedent's balance sheet. An asset-based measure may therefore provide a more comparable and decision-useful measure across insurers. Applying that same principle to unfunded commitments would give analysts an additional perspective on the magnitude of those commitments relative to the insurer's overall asset base.

Accordingly, ACLI recommends that the Handbook include the following as two separate bullets:

- *Review Schedule BA, Part 1, Column 19 total, "Commitment for Additional Investment," as a percentage of total assets, to assess the magnitude of the impact of unfunded commitments on the insurer's liquidity.*

- *Review Schedule BA, Part 1, Column 19 total, "Commitment for Additional Investment," as a percentage of Policyholders' Surplus, to assess the magnitude of the impact of unfunded commitments on the insurer's liquidity.*

This approach preserves the additional perspective FASTWG is seeking from the Policyholders' Surplus measure while providing an exposure-based measure that may facilitate more meaningful comparisons across insurers with differing business models and reinsurance structures.

Illustrative Examples and Risk-Based Tailoring

ACLI appreciates the revisions clarifying that the level of detailed information requested in the Credit Risk Assessment for Unauthorized Reinsurance may depend on the materiality and complexity of the transaction, as well as the assessed likelihood and potential severity of loss after considering collateral, controls, and other mitigating factors. We also appreciate the Working Group's decision to clarify prescriptive provisions as examples.

We recommend reinforcing this risk-focused approach throughout the examples included in both the Credit Risk Assessment for Unauthorized Reinsurance and the Form D Procedures. Information requests, reporting requirements, transaction terms, and approval conditions should be tailored to the nature, structure, complexity, and relevant and material risks of the particular transaction. This would help ensure that the examples are not interpreted as standardized checklists, minimum requirements, or generally preferred regulatory benchmarks.

To make this intent clear, we recommend adding the following introductory language before each example box:

> ***Illustrative Example:*** *The following provisions are examples only, may not be applicable in every situation, and are not intended to establish standardized requirements, minimum thresholds, or regulatory safe harbors.*

This approach would preserve the usefulness of the examples for financial analysts while reinforcing the principles-based and risk-focused nature of the Handbook guidance.

Alignment with the Broader NAIC Reinsurance Initiative

ACLI recognizes that broader consideration of terminology regarding "significant reinsurance arrangements" may extend beyond the scope of this exposure. Once the Financial Condition (E) Committee has addressed Material Transactions, we recommend that FASTWG revisit the related Handbook guidance to assess whether broader revisions are warranted to align terminology and criteria with the Committee's work. That would provide a basis for considering any expansion in scope while helping reduce differing interpretations across states and among analysts and examiners.

Coordinating this review with related NAIC workstreams would help avoid establishing overlapping or potentially different standards through separate Handbook projects. This sequencing is consistent with ACLI's comments on the first exposure encouraging FASTWG to consider the interaction of the Handbook revisions with other ongoing NAIC initiatives and to avoid getting ahead of work that remains under development.

Conclusion

ACLI appreciates the Working Group's consideration of comments on the first exposure and its continued efforts to develop practical, risk-focused guidance for financial analysts. Our additional recommendations are intended to reinforce that analytical procedures, information requests, and transaction-specific conditions should be proportionate to the relevant and material risks presented.

The Handbook's principles-based framework should help regulators identify and understand risk while preserving appropriate supervisory judgment. Avoiding unnecessary duplication and unintended supervisory expectations would further support that purpose.

We appreciate the opportunity to provide these comments and welcome the opportunity to continue working with the Working Group as it considers the revisions.

Sincerely,



Hans Avery
Actuary
hansavery@acli.com
(202) 624-2012



Marc Altschull
Managing Director, Investment and Capital Markets Policy
marcaltschull@acli.com
(202) 624-2089

ATHENE

November 2, 2026

Danielle Smith
Chair, Financial Analysis Solvency Tools (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street
Suite 1500
Kansas City, MO 64106-2197

Via email: RGood@naic.org; RVillegas@naic.org; JMurray@naic.org

Re: Re-exposed Financial Analysis Handbook Revisions

Dear Chair Smith and Members of the Working Group:

Athene Holding Ltd. (Athene) appreciates the opportunity to comment on the Financial Analysis Solvency Tools (E) Working Group's revised draft amendments to the *Financial Analysis Handbook* (Handbook). Athene is a leading retirement services company that issues and reinsures annuity products, helping millions of Americans secure their retirement. We engage constructively with the NAIC and state regulators to support a solvency framework that is transparent, analytically grounded, and calibrated to protect policyholders.

As stated in our September 10, 2026 letter, Athene supports the Working Group's efforts to enhance the reinsurance guidance in the Handbook. The June 16, 2026 referral memorandum from the chairs of the Financial Analysis Working Group, Valuation Analysis Working Group, and Investment Analysis Working Group cited concerns with the emergence of "unauthorized jurisdictions" as growing destinations for life and annuity reinsurance, in contrast to Bermuda. The memorandum specifically referenced "significant concerns with the lack of: 1) defined capital and reserving framework, 2) coherence between permitted accounting, reserving and capital frameworks, 3) transparency and 4) collaboration" in unauthorized jurisdictions. Although the term "unauthorized jurisdiction" is not defined, this appears to be a reference to non-reciprocal jurisdictions.

The Working Group's current draft includes procedures for assessing the risk for "offshore unauthorized reinsurance." The Financial Examiners Handbook (E) Technical Group (FEHTG) has revised its draft amendments to the *Financial Condition Examiners Handbook* to refer to "reinsurers domiciled in jurisdictions presenting additional jurisdictional, transparency, capital, reserving or collateral-related risks." While this language appears intended to align with the intent of the referral, it would presumably require determination by analysts and examiners as to which jurisdictions should be in scope. That could lead to inconsistencies among the states.

We recommend that the Working Group amend the draft language to apply to reinsurers "located outside of reciprocal jurisdictions." This appears to align with the intent of the referral. Reciprocal jurisdiction recognition is a consequential act and the standards to achieve it are demanding. The Financial Condition (E) Committee's July 27 referral to the Life RBC Working Group draws this distinction, directing a new recapture risk factor for reinsurance "located outside of reciprocal jurisdictions." We also recommend that the Working Group coordinate with FEHTG to ensure consistent terminology is used in both handbooks.

Athene appreciates the Working Group's consideration and remains available to support these revisions.

Respectfully submitted,



Kim Welsh
Senior Vice President
Government and Regulatory Affairs
Athene Holding Ltd.

Yellow Highlights – Changes recommended by Commentors that Staff supports accepting after 1st Exposure.
Grey Highlights – Edits recommended by Staff after 1st Exposure.
Blue Highlights – Edits recommended following 2nd Exposure.

----------Detail Eliminated to Conserve Space----------

ANNUAL CREDIT RISK ASSESSMENT

----------Detail Eliminated to Conserve Space----------

Exposure to Private Credit Securities, Level 3 Securities, and Bonds with Private Letter Ratings

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between private placements and emerging private credit strategies when assessing credit risk exposures.

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.

While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types can complicate the assessment of credit quality and reduce the liquidity of the portfolio.

Private credit generally refers to privately negotiated debt or debt-like investments that are not publicly traded. The asset class encompasses a wide range of investment strategies and structures, including private placements, direct lending, private structured assets, asset-based finance, infrastructure debt, commercial real estate debt, and other privately originated credit investments. Asset-based finance encompasses a broad range of transactions secured by identifiable collateral and may exhibit substantially different risk characteristics depending on asset quality, structure, leverage, and credit enhancement features. Therefore, analysts should evaluate asset-based finance exposures based on underlying risk characteristics.

While some private credit strategies focus on middle-market corporate lending, the asset class is considerably broader and includes many investment-grade exposures that have long been utilized by insurance companies. Accordingly, analysts should avoid treating all private credit investments as having similar risk characteristics and

should consider the underlying credit quality, structure, transparency, and valuation methodology of the investment.

"Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. According to Morgran Stanley Investment Management, direct lending comprised 52%[i] ~~is the largest segment and accounts for about 40%~~ of the U.S. private credit market as of Sept. 30, 2025. The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy, more complex investments like feeder fund structures, ~~private credit~~ middle market CLOs with private letter ratings, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property) are expanding.

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities and can make it more difficult to assess credit risk and determine appropriate valuation.
- Less frequent pricing: Private credit may be subject to less frequent valuation and pricing; and it may rely on third-party valuations and/or modeling.
- ~~Assessment of credit quality:~~
    - ~~While lack of transparency can make credit quality more difficult to assess, private credit lenders can often benefit from stronger control over documentation than lending through a syndicate of banks and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.~~
    - ~~Private credit also has the potential to provide a broader pool of debt issuers that results in portfolio diversification.~~
- ~~Future performance~~Risk/Reward Optimization:
    - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.
    - Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
    - Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
    - Diversification benefits through access to issuers and asset types not available in public markets.
    - Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
    - Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.

[i] 52% as of September 2026 per Morgan Stanley Investment Management

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private placements. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves).

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a

single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. Private placements and other established private fixed income investments;
2. Emerging or more complex private credit strategies, including certain direct lending, feeder funds, privately-rated CLO, and asset-based finance structures; and
3. Investments characterized by valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private letter designation rating alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or complex structures.

Procedures / Data

- Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:
    - Complex private credit structures;
    - Securities backed by private letter ratings;
    - Investments with significant Level 3 valuation inputs;
    - Below-investment-grade or unrated private credit exposures; and
    - Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.

- When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk.

    - Ratio of private securities in aggregate, by asset type, and by security code category to total invested assets
    - Ratio of private securities in aggregate, by asset type, and by security code category to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) , and to policyholder surplus (P&C)
    - Change in private securities from the prior year
- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities backed by PLRs (i.e., symbols PL and PLGI).
    - Ratio of securities with PLRs to total invested assets
    - Ratio of securities ~~backed by~~ with PLRs to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
    - Change in securities with ~~backed by~~ PLRs from the prior year

- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 or Level 2D securities to total invested assets
  - Ratio of Level 3 or Level 2D securities to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
  - Change in Level 3 or Level 2D securities from the prior year

Additional Review Considerations

- For insurers with a concentration in bonds with Private Letter Ratings PLRs:
  - ~~Request the support of the NAIC's Securities Valuation Office (SVO) to investigate the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.~~
  - Request details from the company on its own internal ratings for securities with ~~backed by~~ PLRs where applicable and compare with rating agency rating for discrepancies.
- If private placements, private credit investments, Level 3 or 2D securities, or assets with PLRs are material, consider inquiring of the insurer its infrastructure and investment management policies and procedures (i.e. portfolio management and credit analyst expertise, including approach to making investment decisions) in place either internally, or via an affiliate, and/or outsourced investment manager, to manage these investments.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
-
- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

----------Detail Eliminated to Conserve Space----------

Inadequate Collateral for Mortgage Loan Risk

An important consideration in the analysis of mortgage loans is the adjusted loan-to-value and debt service coverage ratio for each property owned, which are used in the determination of the mortgage's Commercial Mortgage Risk Category and are detailed in the RBC worksheet. Out-of-date appraisals may result in inaccurate valuation, resulting in an undervalued underlying collateral asset.

Procedures / Data

- Review information available in the RBC filing (LR004) and Schedule B detail to identify a concentration in loans with unfavorable debt service coverage (DSC) ratios and adjusted loan-to-values (LTV) (i.e., book value/recorded investment of each loan compared to the value of the land and buildings mortgaged) of the individual mortgage loans to determine whether the mortgage loans, and ~~or~~ in particular office property types (as of 2026) are adequately collateralized.

Additional Review Considerations

- For mortgage loans with interest overdue or in process of foreclosure, review the date of the last appraisal or valuation (Schedule B – Part 1) to determine whether updated appraisals should be obtained.
- If significant or concerning concentrations in mortgage loans with unfavorable DSC or LTV ratios or ~~in~~ office property types are identified, request additional information from the insurer to further assess their credit risk in this area and evaluate any risk mitigation strategies in place.

Traditional investment-grade private placements and mortgage-related investments that are addressed elsewhere in the Handbook generally should not be considered elevated-risk private credit exposures solely because they are privately originated, privately negotiated, or less liquid than comparable public securities. Additional scrutiny should focus on investments exhibiting heightened complexity, valuation uncertainty, lower credit quality, or nontraditional structures.

----------Detail Eliminated to Conserve Space----------

Credit Quality of Assets Supporting Collateral Loans (Life/A&H Insurers)

The procedure assists analysts in determining whether concerns exist due to the level of investment in collateral loans. Collateral loans are unconditional obligations for the payment of money secured by the pledge of an investment. While collateral loans are exposed to the market and credit performance of their underlying collateral, they are debt instruments that incorporate structural credit enhancements, including overcollateralization, diversification, cross-collateralization, and lender protections, which reduce economic risk relative to direct ownership of the underlying assets. Market conditions such as rising interest rates and market volatility can impact the value of the underlying collateral and, in turn, an insurer's ability to fulfill policyholder obligations. However, interest rates, while still relatively high (as of 2026), were lowered for the first time in almost a year, and collateral loans are not a core investment for U.S. insurance companies. Analysts should review Annual Financial Statement, Schedule BA. In most states, collateral loans are required to be secured or collateralized by assets which have a value in excess of the amount of the loan and which are considered admitted assets for an insurer.

Procedures / Data

- Review the following ratios to determine the level of concentration in collateral loans.
  - Ratio of collateral loans to total net admitted assets.
  - Ratio of collateral loans to capital and surplus plus AVR.

Additional Review Considerations

- Compare the fair value of the collateral to the amount loaned to determine whether the loan is adequately collateralized. In those instances where the underlying collateral is comprised of securities, analysts might consider verifying the rate used to obtain the fair value of the securities by referencing the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual).
- Review Annual Financial Statement, Schedule BA – Other Invested Assets Owned and perform the following for each such loan:
  - Determine whether the collateral for the loan is invested in a quality asset.

- Determine whether the collateral loan is to an officer, director, parent, subsidiary, or affiliate.

----------Detail Eliminated to Conserve Space----------

Impairment of Invested Assets Exposed to Climate Change and/or Transition Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include oil/gas, transportation, heavy manufacturing, and agriculture. The insurer's investment portfolio is subject to prospective devaluation or impairment of the assets or changes in the asset return associated with its holdings of climate-affected assets.

Procedures / Data

- Review the information disclosed by the insurer in its responses to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review other relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10K or 10Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Additional Review Considerations

- Review the insurer's investment policies and strategies to assess whether material climate change, transition and asset devaluation risk considerations have been appropriately implemented into the investment processes.
- Review the most recent examination report and summary review memorandum (SRM) for any findings regarding climate change/energy transition risks.
- If concerns exist, consider requesting information from the insurer regarding its management of exposure to material climate change/energy transition risk, including how it identifies and estimates current and prospective exposures and the limits (if any) in place to avoid concentrations.

----------Detail Eliminated to Conserve Space----------

Credit Quality, Adequacy and Appropriateness of Assets Held for Modco or FWH Agreements (Life/A&H Insurers)

Concerns may exist regarding the quality, adequacy and appropriateness of assets held to support Modified Coinsurance (Modco) or Funds Withheld (FWH) reinsurance, particularly as investments become increasingly complex. Concerns may include controls and governance over investment practices, valuation and ratings of assets, and if material amounts of assets involve related party transactions.

Where collateral held is related to Modco and FWH reinsurance, the analyst should review the information in Note to the Financials #5L(1), #5L(4) and #5L(5), and Schedule S—Part 8—Reinsurance Agreements with Funds Withheld and Modified Coinsurance, in conjunction with other credit, operational and strategic risk of the insurer's reinsurance program. Additionally, review the analysis considerations related reserve reporting required by AG 53 (complex assets) and AG 55 (assets supporting reinsurance) outlined in the Reserving Risk Assessment and SOA procedures and guidance.

Where the company is engaged in material Modco and FWH arrangements, the analyst can use the detail of collateral received and held under Note 5L(4) to identify the types of assets held by investment schedule, and gain an understanding of the materiality of aggregate BACV of the collateral received to the insurer's asset portfolio. Further, the Note #5L(5) disclosure identifies if securities held as collateral under Modco or FWH agreements are also pledged under other arrangements, in which case they would not be for the benefit of the reinsurer or available to fulfill the liabilities of the reinsurance contract. The analyst can use the information in Schedule S—Part 8 to identify any concerns with the types of assets and credit quality of assets held under ceded or assumed Modco or FWH agreements.

Procedures / Data

- Identify the types of reinsurance agreements and jurisdiction of the reinsurer [Annual Financial Statement, Schedule S – Part 3] and determine if concerns may exist over the adequacy and quality of assets held by reinsurers in support of ceded reserves that may require further analysis or inquiry to the insurer.
- Compare the BACV of the collateral received and assets held under Modco/FWH Reinsurance Agreements to the recognized obligation for Modco and FWH assets. [Annual Financial Statement, Notes to the Financials #5L(4)(m and n)].
- Identify if investments held under FWH agreements (including Modco) are related to the Modco/FWH reinsurer [Annual Financial Statement, Notes to the Financials 5L(5)(o-v)].
- Identify if the insurer is engaged in ceding business under Modco and FWH agreements with offshore reinsurers.
    - Gain an understanding, through review of Schedule S - Part 3, of the types of insurance business ceded, the reinsurer's jurisdiction, if affiliated or non-affiliated, and applicable collateral requirements by type of reinsurer (i.e. authorized, unauthorized, reciprocal jurisdiction, certified)
- Review Schedule S – Part 8 to determine if concerns exist regarding the types of assets held or the credit quality of assets held under Modco/FWH agreements. Consider if the aggregate of medium or lower quality assets held represent a material amount of the related Modco/FWH liabilities.
    - Review Schedule S – Part 8 in comparison to Life RBC (asset schedules) to ensure asset subtotals match. If differences exist, inquire of the insurer, as differences may have an impact on the RBC calculation.
- Determine if assets held under Modco or FWH agreements are also pledged under other agreements [Annual Financial Statement, Notes to the Financials #5L(5)].

- Determine if assets held under Modco or FWH agreements contain a material amount of private credit assets or related party investments (or related to the reinsurer managing the portfolio). If so, consider additional procedures in the Private Credit section above and/or Related Party section below.

----------Detail Eliminated to Conserve Space----------

Collectability or Default of Investments Involving Related Parties

Determine related party exposure in the investment portfolio and assess any related credit risk.

Related parties are entities that have common interests as a result of ownership, control, affiliation or by contract as definited in *SSAP No. 25—Affiliates and Other Related Parties* (SSAP No. 25). Refer to the *Insurance Holding Company System Model Act* (Model #440) and SSAP No. 25 for a broader definition of "affiliate," "related party" and "control".

Related party transactions are subject to abuse because reporting entities may be induced to enter transactions that may not reflect economic realities or may not be fair and reasonable to the reporting entity or its policyholders. As such, related party transactions require specialized accounting rules and increased regulatory scrutiny.

The anlayst should utilize the tools available in iSite+ to identify if the insurer has a material exposure to investments involving related parties, either on an asset category basis or in aggregate, and by the related party designation noted below. If a material exposure exists, further assessment of the credit risk may be warranted. For example, what is the NAIC designation of investments involving related parties? Analysts may also consider the extent to which related parties are involved in securitizing or originating business for the insurer, and what differences may exist in how investments involving related parties are valued (market risk). If the role of the related party is that of a third-party advisor, factors to consider may include for example, the expertise of the related party advisor, any potential conflicts of interest, and if related parties are originating investments only for the insurer or also to the public, the latter being subject to SEC requirements.

Within the Annual Financial Statement investment Schedules B, BA, D, DA, DB, DL, and E (Part 2), all investments involving related parties must incude disclosure to ensure full transparency. This disclosure is in the column "Investments Involving Related Parites". It designates investments by the following roles:

1. Direct loan or direct investment (excluding securitizations) in a related party, for which the related party represents a direct credit exposure.
2. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer, or other similar influential role and for which 50% or more of the underlying collateral represents investments in or direct credit exposure to related parties.
3. Securitization or similar investment vehicles such as mutual funds, limited partnerships and limited liability companies involving a relationship with a related party as sponsor, originator, manager, servicer, or other similar influential role and for which less than 50% (including 0%) of the underlying collateral represents investments in or direct credit exposure to related parties.
4. Securitization or similar investment vehicles such as mutual funds, limited partnerships, and limited liability companies in which the structure reflects an in-substance related party transaction but does not involve a relationship with a related party as sponsor, originator, manager, servicer, or another similar influential role.
5. The investment is identified as a related party, but the role of the related party represents a different arrangement than the options provided in choices 1-4.
6. The investment does not involve a related party.

Procedures / Data

- Review the Annual Financial Statement investment schedules, as disclosed in the column "Investments Involving Related Parties" and utilizing iSite+ tools, determine if the insurer has material related party exposures in its investment portfolio. This disclosure is included in:
  - Schedule B – Part 2
  - Schedule BA – Part 2
  - Schedule D – Part 1, Sections 1 and 2
  - Schedule DA – Part 1
  - Schedule DB – Part A Section 1
  - Schedule DL – Part 1 and 2
  - Schedule E, Part 2

  Consider exposure by asset class and in aggregate, and by the role of the related party in the investment as designed by the "Investments Involving Related Parties" disclosure.
- If concerns exist regarding a material related party exposure in the investment portfolio, assess the credit quality of those investments and assess any historical default experience.
- Determine if related party investments include a material amount of private credit assets (e.g. related investment manager or related reinsurer managing the Modco/FWH reinsurance assets). If so, consider additional procedures in the Private Credit or Modco/FWH sections above.

Yellow Highlights – Changes recommended by Commentors that Staff supports accepting after 1st Exposure.
Grey Highlights – Edits recommended by Staff after 1st Exposure.
Blue Highlights – Edits recommended following 2nd Exposure.

LIQUIDITY RISK: Inability to meet contractual obligations as they become due because of an inability to liquidate assets or obtain adequate funding without incurring unacceptable losses.

The Liquidity Risk Assessment is focused primarily on overall liquidity, liquidity of investments, receivables, and cash flow from operations. In analyzing liquidity risk, analysts may analyze specific types of investments and receivables held by insurers. An analyst's risk-focused assessment of liquidity risk should take into consideration the following areas (but not be limited to):

- Liquidity ratios/metrics
- Liquidity of certain investments with limited trading and limited public information, such as: private credit securities, including private placement bonds; common stock; highly structured investments; investments on Schedule BA; and affiliated investments
- Liquidity of certain receivables, including health care receivables and special deposits
- Cash flow from operations
- Stockholder dividends
- Surrender and withdrawal activity for life insurers

----------Detail Eliminated to Conserve Space----------

Impact of Market Volatility on the Liquidity of the Aggregate Investment Portfolio

An important consideration when markets experience significant volatility and strains is the potential negative impact may not be on just one or a small number of investments held by insurers. Rather, market strains can have a significant impact on an entire asset class, several asset classes, or the entire investment portfolio. Particularly vulnerable are asset classes ~~that represent smaller~~ in markets that are typically less liquid, are ~~more~~ structurally complex or are assets that would be considered ~~less traditional~~ atypical for insurers. Therefore, state insurance regulators should consider the potential impact of significant market challenges on different asset classes in the investment portfolios of insurers.

Procedures

- Review and monitor material asset classes for significant changes in fair value and/or significant changes in relative liquidity. Utilize data in the Annual Statement, Financial Profile, Snapshot Investment Summary and investment dashboards. Also refer to specific liquidity guidance in this chapter on asset groups such as bonds, BA assets and mortgage loans. Do not limit considerations to one asset class but also consider

the aggregate of all such vulnerable asset classes. Examples of asset groupings that may represent notable exposures in insurer portfolios and that should be considered are:

- Below investment grade bonds (rated below BBB-/baa3).
- ~~Weaker investment grade ("BBB" rated) bonds.~~
- Commercial mortgage loans, ~~particularly~~ for example office properties (in the current market as of 2026).
- Mezzanine loans.
- Real estate equity.
- Structured securities, especially collateralized loan obligation (CLO) tranches (including CLO Combo Notes and Middle Market CLOs).
- Residential mortgage-backed securities (RMBS), specifically as to cash flow variability.
- Emerging markets investments.
- Hedge funds.
- Private equity funds.
- Private credit, including private placements (specifically non-144A) and private letter ratings.
- Derivatives transactions.
- Concentrations in exposure to sectors impacted by the current market, currently the auto, technology, consumer products and retail sectors, due to technology/software (AI), and energy, due to high oil prices ~~the potential impact of tariffs~~.

The materiality of these exposures should be evaluated in the context of the insurer's overall risk profile, including applicable NAIC capital requirements associated with the assets. Different situations may call for different materiality standards, so it is important to be able to explain the standard used.

When evaluating the liquidity of less liquid assets, analysts should consider the insurer's broader asset-liability management framework. Life insurers for example, generally have long investment horizons due to the long-duration and generally predictable nature of their liabilities. Accordingly, insurers actively model asset and liability cash flows to ensure sufficient liquidity is available to meet policyholder obligations as they come due. Insurers generally do not invest in less liquid assets, including private equity, hedge funds, private credit, and commercial mortgage loans, for day-to-day liquidity management. Rather, the ability to allocate a portion of the portfolio to ~~such~~ assets is a structural feature of the insurance business model that can be a source of additional investment income while remaining consistent with prudent liquidity management.

- Refer to the Procedures for review of Actuarial Guideline 53 and Actuarial Guideline 55 in the Reserve Risk Chapter for additional related investment liquidity review.

Additional Review Considerations

i. For ~~the~~ identified asset classes ~~above~~, where there is not a readily available or exchange traded market, verify pricing and valuation sources and corresponding valuation methods. Close attention should be given to asset classes like private equity and real estate that usually report on a 3-month lag, as well as private credit whose valuations may be subjective.

ii. Inquire as to how the insurer is managing the potential risk of rating migration. Inquire as to how they may apply a credit rating transition matrix and calculate the resulting increased RBC charges.

iii. Inquire as to how the insurer is managing the above-mentioned challenges and other potential challenges in the investment marketplace. For example, consider the following questions:
   a. How is the insurer managing its liquidity needs given the changes in investment markets, including when/if ~~especially given~~ historically liquid assets may not be as liquid?
      1. How is the insurer managing changes in cash-flow expectations from prepayments (which are more likely when interest rates are decreasing), both generally and specifically associated with structured ~~mortgage-backed~~ securities?
   b. How is the insurer managing significant changes in fair value of portfolio assets, especially for longer dated investments?
      1. Are other-than-temporary- impairments (OTTI) appropriate?
      2. If there is an ongoing risk, should the insurer consider shortening the duration of future investments?

iv. Review the insurer's Liquidity Stress Test submission (if applicable) to evaluate results and assess the insurer's stress testing process and assumptions for reasonableness.

v. Inquire as to how changes in the investment profile (particularly duration) may impact asset/liability matching, asset adequacy analysis and cash-flow testing.

~~vi. Request an Opinion from the NAIC's Securities Valuation Office (SVO) or Structured Securities Group (SSG) on a specific investment holding or transaction. A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.~~

vii. Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio of investment risk exposures and obtain additional follow-up procedures that can be performed by the department to address any overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

----------Detail Eliminated to Conserve Space----------

Exposure to Private Credit Securities, Level 3 Securities, Bonds with Private Letter Ratings and Unfunded Commitments

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more

complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between private placements and emerging private credit strategies when assessing credit risk exposures. ~~In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs.~~

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.

While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types ~~the potential lack of transparency related to private assets~~ can complicate the assessment of credit quality and increase the liquidity risk of the portfolio.

~~Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited—access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, they are more susceptible to economic downturns and the impact of rising interest rates.~~

Private credit generally refers to privately negotiated debt or debt-like investments that are not publicly traded. The asset class encompasses a wide range of investment strategies and structures, including private placements, direct lending, private structured assets, asset-based finance, infrastructure debt, commercial real estate debt, and other privately originated credit investments. Asset-based finance encompasses a broad range of transactions secured by identifiable collateral and may exhibit substantially different risk characteristics depending on asset quality, structure, leverage, and credit enhancement features. Therefore, analysts should evaluate asset-based finance exposures based on underlying risk characteristics.

While some private credit strategies focus on middle-market corporate lending, the asset class is considerably broader and includes many investment-grade exposures that have long been utilized by insurance companies. Accordingly, analysts should avoid treating all private credit investments as having similar risk characteristics and should consider the underlying credit quality, structure, transparency, and valuation methodology of the investment.

~~Private credit has~~ "Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. ~~Direct~~ According to Morgran Stanley Investment Management, direct lending comprised 52%[i] ~~is the largest segment and accounts for about 40%~~ of the U.S. private credit market as of Sept. 30, 2025. The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy, ~~type of private credit , it is evolving into~~ more complex investments like feeder fund structures, ~~private credit~~ middle market CLOs with private letter ratings, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property) are expanding.

[i] 52% as of September 2026 per Morgan Stanley Investment Management

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities and can make it more difficult to assess credit risk and determine appropriate valuation.
- Less frequent pricing: Private credit may be subject to less frequent valuation and pricing; and it may rely on third-party valuations and/or modeling, ~~which may be subjective~~.
- ~~Assessment of credit quality:~~
    - ~~While lack of transparency can make credit quality more difficult to assess,private credit lenders can often benefit from stronger control over documentation, as compared to a syndicate of lenders, and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.~~
- Private credit can contribute to an investment portfolio's diversification, with respect to issuers and duration, among other factors ~~also has the potential to provide a broader pool of debt issuers that results in portfolio diversification.~~
- ~~Future performance~~Risk/Reward Optimization:
    - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.
    - ~~As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.~~
    - Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
    - Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
    - Diversification benefits through access to issuers and asset types not available in public markets.
    - Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
    - Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private placements. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided

in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves). Level 2D reflects use of internal models.

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

When reviewing Level 3 assets, analysts should distinguish valuation classification from credit risk assessment. The fair value hierarchy is intended to identify the nature of inputs used to measure fair value, not to assign a credit risk classification. Therefore, a Level 3 classification reflects the use of a significant number of unobservable inputs and should not be interpreted, on its own, as evidence of elevated credit risk. Certain long-duration insurance assets may have limited observable market inputs but still exhibit stable contractual cash flows and strong credit characteristics. In addition, some assets may be classified as Level 3 because observable valuation inputs are not available at the measurement date, and those assets may subsequently migrate to Level 2 once observable inputs become available.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a

single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

When reviewing securities that have been assigned PLRs, analysts should consider that the growth in PLRs is largely a reflection of increased private market issuance and the continued evolution of private credit markets, rather than, by itself, an indication of deteriorating credit quality. As market activity shifts toward newer private credit asset classes, the use of PLRs may increase because these assets are often issued in private markets and may not be broadly or publicly rated or publicly disseminated. Analysts should also consider the insurer's broader credit assessment framework, including internal underwriting, investment committee review, and ongoing surveillance, as ~~investments in~~ private assets generally do not rely ~~solely~~ on agency ratings for credit evaluation.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. Private placements and other established private fixed income investments;
2. Emerging or more complex private credit strategies, including certain direct lending, feeder funds, privately-rated CLO, and asset-based finance structures; and
3. Investments characterized by valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private letter designation rating alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or complex structures.

Unfunded Private Equity Commitments

Insurers have continued to expand their allocations to private equity, as evidenced by the increase in unfunded commitment (liability) levels in recent years. These funding commitments—contractual obligations to contribute capital to private equity funds over time—have grown along with insurers' appetite for higher-yielding, long-duration assets amid heightened market volatility. This trend underscores a strategic shift toward private markets, although it also introduces additional considerations around liquidity management and possible valuation uncertainty. Unfunded commitments may be commitments to private credit funds, but can also include commitments to private equity, hedge funds and real estate limited partnerships.

Private equity and private credit limited partnership agreements typically include a funding commitment, which may require the limited partners to reserve a significant amount of liquid assets to meet funding calls. Failure to meet a funding call could result in severe penalties. This could significantly impair the insurer's liquidity, as any reserved funds would not be readily available to pay the insurer's other obligations.

Analysts should evaluate whether the insurer has incorporated those commitments into its liquidity planning, cash-flow forecasting, and overall asset-liability management process.

<u>Procedures / Data</u>

- Ratio of private-placement bonds owned to policyholder surplus (P/C), to capital and surplus plus AVR (Life/A&H) and to capital and surplus (Health)

- Increase in private placement bonds from the prior year
  - Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:
    - Complex private credit structures;
    - Securities backed by private letter ratings;
    - Investments with significant Level 3 valuation inputs;
    - Below-investment-grade or unrated private credit exposures; and
    - Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.
    - When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk
    - ~~Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.~~
  - Ratio of private securities in aggregate by asset type, and by security code category to total invested assets
  - Ratio of private credit securities in aggregate, by asset type, and by security code category to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)
  - Change in private securities from the prior year
- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities ~~backed by~~ with PLRs (i.e., symbols PL and PLGI).
  - Ratio of securities with PLRs to total invested assets
  - Ratio of securities ~~backed by~~ with PLRs to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) and policyholder surplus (P&C)
  - Change in securities ~~backed by~~ with PLRs from the prior year, in aggregate and by asset type
- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 or Level 2D securities in aggregate to total invested assets
  - Ratio of Level 3 or Level 2D securities in aggregate and by asset type, to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) and policyholder surplus (P&C)
  - Change in Level 3 or Level 2D securities from the prior year, in aggregate and by asset type
- Review Note 14A1 to identify if the insurer has a material exposure to contingent commitments.
  - Change in contingent commitments (liabilities) since the prior year, in aggregate.
- Review Schedule BA Part 1, Column 19 total—Commitment for Additional Investment, as a percentage of Policyholders' Surplus, to assess the magnitude of the impact of unfunded commitments on the insurer's liquidity.
- Review Schedule BA Part 1, Column 19 total—Commitment for Additional Investment, as a percentage of total assets, to assess the magnitude of the impact of unfunded commitments on the insurer's liquidity.

Additional Review Considerations

- Review Note 14 – Liabilities, Contingencies, and Assessments, to assess the insurer's exposure to unfunded commitments to private credit funds.
- If exposure to unfunded commitments is significant, consider whether the insurer's management and board have a clear understanding of differences in liquidity and market value drivers, as well as the reasons for

different yield and cash-flow characteristics, as unfunded commitments contractually obligate the insurer to contribute capital to private equity funds over a designated period of time.

- Review Annual Financial Statement, Schedule D – Part 1A to determine the amount, issue type, NAIC designations, maturity distribution of privately-placed bonds owned, and the amount of privately placed bonds that are freely tradeable under U.S. Securities and Exchange Commission (SEC) Rule 144 or qualified for resale under SEC Rule 144A.
- For insurers with a concentration in bonds with Private Letter Ratings (PLRs):
  - ~~Request the support of the NAIC's Securities Valuation Office (SVO) to identify the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.~~
  - Request details from the company on its own internal ratings for securities ~~backed by~~ with PLRs where applicable and compare with rating agency rating for discrepancies.
- For insurers with a significant concentration in Level 3 or Level 2D securities, consider reviewing the investment schedule detail to identify whether the investments with Level 3 or Level 2D fair values are private, whether a private letter rating is the source of the NAIC designation for these items, and the extent the investments have aggregate deferred interest or paid-in-kind (PIK) interest.
- Utilize information on fair value hierarchy reported in the investment schedules to identify individual securities warranting additional review.
- If private placements, private credit investments, Level 3 or 2D securities, or assets with PLRs are material, consider inquiring of the insurer its infrastructure and investment management policies and procedures (i.e. portfolio management and credit analyst expertise, including approach to making investment decisions) in place either internally, or via an affiliate, and/or outsourced investment manager, to manage these investments.
- Consider requesting additional information on the ongoing performance of these assets and/or the pricing assumptions and methodologies used in fair value measurement.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
- ~~If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~
- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

----------Detail Eliminated to Conserve Space----------

Invested Asset Exposure to Climate Change, Transition and Asset Devaluation Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks and asset devaluation risk. The insurer's investment portfolio is subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include, oil/gas, transportation, heavy manufacturing, and agriculture. In assessing an insurer's exposure to these risks, the analyst is encouraged to review information disclosed by the insurer in its responses to the NAIC's Climate Risk Disclosure Survey, U.S. Securities and Exchange Commission (SEC) filings, and/or the Own Risk and Solvency Assessment (ORSA) Summary Report filings. In addition, the analyst is encouraged to review the results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings (U.S. Insurance Industry Climate Affected Investment Analysis) to identify potential concentrations in exposure.

Procedures

- Review information provided in the insurer's response to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review information provided in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Yellow Highlights – Changes recommended by Commentors to the CR and LQ chapter that Staff supports accepting from 1st Exposure.
Grey Highlights – Edits recommended by Staff after 1st Exposure.
Blue Highlights – Edits recommended following 2nd Exposure.

----------Detail Eliminated to Conserve Space----------

ANNUAL MARKET RISK ASSESSMENT

----------Detail Eliminated to Conserve Space----------

Significant Investment Concentration by Asset Class

Determine whether the insurer's investment portfolio appears to be adequately diversified to avoid an undue concentration of investments by asset type, duration or issuer.

Various types of investments to total net admitted assets (excluding separate accounts for Life/A&H) are a measure of the diversity of the insurer's investment portfolio by type of investment. The results of these ratios may also provide some indication of the insurer's liquidity. In addition, the ratio of the investment in any one issuer to total net admitted assets (excluding separate accounts for Life/A&H) is a measure of the diversity of the insurer's investment portfolio by issuer.

For foreign securites, market risk may include material exposures that could result in credit losses if those investments are affected by negative changes in geopolitical or foreign economic environments.

For mortgage loans, market risk may include the risk that the insurer is not properly identifying, handling and recording foreclosed mortgage loans.

Procedures/Data

- Consider evaluating the following assets classes in comparison to total admitted assets[i] to determine the level of concentration *(See also Credit Risk Assessment for diversification of other asset classes):*
  - Asset-Backed Securities.
  - Foreign bonds.
  - Common stocks.
  - Mortgage loans.
  - Real Estate (before encumbrances), including home office real estate.
  - Total derivatives (notional value).
  - Investment in affiliates.
  - Any one single investment in foreign bonds, common stock, real estate and derivatives (excluding afiliated investments) *(Note that single investments in financial asset-backed securities are considered within the Credit Risk Assessment).*

Additional Review Considerations

- Review the percentage distribution of assets for significant shifts in the mix of investments owned during the past five years.

[i] For ratios in this asset concentration procedure, net admitted assets excludes separate accounts for Life/A&H.

- Industry and Peer Comparison: Note that comparisons should be based on insurer type, but also should reflect the size of the company and more specific aspects of the insurer's liabilities.
    - Compare the insurer's distribution of cash and invested assets and recent changes in asset categories, with a particular focus on the last year or the previous few years, to industry averages and peer averages utilzing iSite+ tools to determine significant deviations from the industry averagesand comparison to peer companies.
    - Compare the insurer's investment portfolio to an appropriate peer group. Consider using the NAIC Peer Analysis Financial Profile report or the Snapshot Investment Summary in iSite+ to identify an compare to an appropriate group of peer companies for this purpose.
- If the insurer's investments include a significant amount of foreign bonds, review the Annual Supplemental Investment Risks Interrogatories (#4 through #11). Consider the insurer's potential foreign currency exposure from holding bonds denominated in a foreign currency.
- Review of the Annual Supplemental Investment Risks Interrogatories to identify any unusual items or areas and determine whether the insurer's investment portfolio is adequately diversified to avoid significant aggregate market risk.
- Review of the Legal Risk Assessment to determine whether the insurer's investment portfolio is in compliance with the investment limitations and diversification requirements per the state's insurance laws.
- Review the most recent examination report and Summary Review Memorandum (SRM) for any findings regarding market risks associated with investment concentration and exposure to riskier asset classes.
- Inquire of the insurer its planned asset mix, and diversification strategies.

----------Detail Eliminated to Conserve Space----------

Impact of Market Volatility on the Aggregate Investment Portfolio

An important consideration when markets experience significant volatility and strains is the potential negative impact may not be on just one or a small number of investments held by insurers. Rather, market strains can have a significant impact on an entire asset class, several asset classes, or the entire investment portfolio. Particularly vulnerable are asset classes in ~~that represent smaller~~ markets that are typically less liquid, are ~~more~~ structurally complex or are assets that would be considered ~~less traditional~~ atypical for insurers. Therefore, state insurance regulators should consider the potential impact of significant market challenges on different asset classes in the investment portfolios of insurers.

Procedures

- Review and monitor material asset classes for significant changes in fair value and/or significant changes in relative liquidity. Utilize data in the Annual Statement, Financial Profile, Snapshot Investment Summary and investment dashboards. Also refer to specific liquidity guidance in this chapter on asset groups such as bonds, BA assets and mortgage loans. Do not limit considerations to one asset class, but also consider the aggregate of all such vulnerable asset classes. Examples of asset groupings that may represent notable exposures in insurer portfolios and that should be considered are:
    - Below investment grade bonds. (rated below BBB-/baa3).
    - ~~Weaker investment grade ("BBB" rated) bonds.~~

- Commercial mortgage loans, ~~particularly~~ for example office properties (in the current market as of 2026).
- Mezzanine loans.
- Real estate equity.
- Structured securities, especially collateralized loan obligation (CLO) tranches (including CLO Combo Notes and Middle Market CLOs).
- Residential mortgage-backed securities (RMBS), specifically as to cash flow variability.
- Emerging markets investments.
- Hedge funds.
- Private equity funds.
- Private credit, including private placements (specifically non-144A) and private letter ratings.
- Derivatives transactions.
- Concentrations in exposure to sectors impacted by the current market, currently the auto, technology, consumer products and retail sectors due to technology/software (AI), and energy, due to high oil prices ~~the potential impact of tariffs.~~

The materiality of these exposures should be evaluated in the context of the insurer's overall risk profile, including applicable NAIC capital requirements associated with the assets. Different situations may call for different materiality standards, so it is important to be able to explain the standard used.

When evaluating the liquidity of less liquid assets, analysts should consider the insurer's broader asset-liability management framework. Life insurers for example, generally have long investment horizons due to the long-duration and generally predictable nature of their liabilities. Accordingly, insurers actively model asset and liability cash flows to ensure sufficient liquidity is available to meet policyholder obligations as they come due. Insurers generally do not invest in less liquid assets, including private equity, hedge funds, private credit, and commercial mortgage loans, for day-to-day liquidity management. Rather, the ability to allocate a portion of the portfolio to ~~such~~ assets is a structural feature of the insurance business model that can be a source of additional investment income while remaining consistent with prudent liquidity management.

Additional Review Considerations

- For ~~the~~ identified asset classes ~~above~~, where there is not a readily available or exchange traded market, verify pricing and valuation sources and corresponding valuation methods. Close attention should be given to asset classes like private equity and real estate that usually report on a 3-month lag, as well as private credit whose valuations may be subjective.

- Inquire as to how the insurer is managing the potential risk of rating migration. Inquire as to how they may apply a credit rating transition matrix and calculate the resulting increased RBC charges.

- Inquire as to how the insurer is managing the above-mentioned challenges and other potential challenges in the investment marketplace. For example, consider the following questions:
  - How is the insurer managing significant changes in fair value of portfolio assets, especially for longer-dated investments?
  - Are other-than-temporary- impairments (OTTI) appropriate?
  - If there is an ongoing risk, should the insurer consider shortening the duration of future investments?

- Review the insurer's Liquidity Stress Test submission (if applicable) to evaluate results and assess the insurer's stress testing process and assumptions for reasonableness.

- Inquire as to how changes in the investment profile (particularly duration) may impact asset/liability matching, asset adequacy analysis and cash-flow testing.

- ~~Request an Opinion from the NAIC's Securities Valuation Office (SVO) or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~

- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio of investment risk exposures and obtain additional follow-up procedures that can be performed by the department to address any overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

Exposure to Private Credit Securities, Level 3 Securities, Bonds with Private Letter Ratings and Unfunded Commitments

In recent years, the insurance industry has seen an ongoing increase in the amount and diversity of private fixed income investments held by U.S. domestic insurers. Private fixed income encompasses a broad range of asset types, including traditional investment-grade private placements, private structured assets, direct lending, and other credit-oriented investments. Many of these investments have been longstanding components of insurer portfolios and are generally well suited to insurers' long-duration liabilities and investment horizons.

The ability to invest in less liquid assets is a structural feature of the insurance business model and allows insurers to earn an illiquidity premium while continuing to meet policyholder obligations. While certain newer and more complex private credit structures may warrant enhanced regulatory attention, analysts should distinguish between private placements and emerging private credit strategies when assessing credit risk exposures.

~~In recent years, the insurance industry has seen an ongoing increase in the amount of private assets held by U.S. domestic insurers, including securities with NAIC designations supported by private letter ratings and securities that are valued based on Level 3 (unobservable) inputs.~~

Potential areas of focus may include investments that involve heightened complexity, limited transparency, reliance on unobservable valuation inputs, private letter ratings, or nontraditional structures.
While this increase is generally consistent with the broader capital markets trend of increased issuance of private assets, their relative opacity versus other asset types ~~the potential lack of transparency related to private assets~~ can complicate the assessment of credit quality and increase the liquidity risk of the portfolio.

~~Private credit generally refers to debt, or debt-like, securities that are not publicly issued or traded. Private credit is an evolving, alternative funding source. Non-bank lenders, including insurance companies, private debt funds, and business development companies, issue private loans directly to mostly small and middle-market companies that do not have—or have limited—access to the public corporate bond and loan markets. These small middle-market companies often have more debt than larger companies that access capital via leveraged loans and public bonds and, therefore, they are more susceptible to economic downturns and the impact of rising interest rates.~~

Private credit generally refers to privately negotiated debt or debt-like investments that are not publicly traded. The asset class encompasses a wide range of investment strategies and structures, including private placements, direct lending, private structured assets, asset-based finance, infrastructure debt, commercial real estate debt, and other privately originated credit investments. Asset-based finance encompasses a broad range of transactions secured by identifiable collateral and may exhibit substantially different risk characteristics depending on asset quality, structure, leverage, and credit enhancement features. Therefore, analysts should evaluate asset-based finance exposures based on underlying risk characteristics.

While some private credit strategies focus on middle-market corporate lending, the asset class is considerably broader and includes many investment-grade exposures that have long been utilized by insurance companies. Accordingly, analysts should avoid treating all private credit investments as having similar risk characteristics and should consider the underlying credit quality, structure, transparency, and valuation methodology of the investment.

~~Private credit has~~ "Private credit" describes a variety of strategies that include direct lending, distressed debt, venture debt, mezzanine finance, and special situations. ~~Direct~~ According to Morgran Stanley Investment Management, direct lending comprised 52%[ii] ~~is the largest segment and accounts for about 40%~~ of the U.S. private credit market as of Sept. 30, 2025.The largest investors in private credit are typically pension funds, insurance companies, and sovereign wealth funds. While direct lending to corporate issuers is the simplest and most common strategy ~~type of private credit, it is evolving into~~ more complex investments like feeder fund structures, ~~private credit~~ middle market CLOs with private letter ratings, and asset-based financing (where loans are secured by collateral such as inventory, receivables, equipment, or property).

Risks and mitigating factors include:

- Less liquidity: Private credit is generally issued directly by a non-bank lender or a small group of lenders, resulting in a relatively illiquid market where secondary trading is limited.
- Less transparency: The availability of information about a private credit security is often contractually restricted, which contributes to lower transparency compared to public securities and can make it more difficult to assess credit risk and determine appropriate valuation.
- Less frequent pricing: It may be subject to less frequent valuation and pricing.
- ~~Assessment of credit quality:~~
    - ~~While lack of transparency can make credit quality more difficult to assess, private credit lenders can often benefit from stronger control over documentation and are able to customize terms of the transaction given their direct relationship with borrowers. In the event of stress, lenders and~~

[ii] 52% as of September 2026 per Morgan Stanley Investment Management

~~investors should be able to work directly with the borrower to modify the transaction terms or add investor safeguards.~~

- Private credit can contribute to an investment portfolio's diversification, with respect to issuers and duration, among other factors ~~it also has the potential to provide a broader pool of debt issuers that results in portfolio diversification~~.

- ~~Future performance~~Risk/Reward Optimization:
  - Private credit generally offers higher spreads and yields than public corporate bonds and loans to compensate investors for the relative market illiquidity (lack of a secondary market) and complexity depending on the transaction type.
  - ~~As the nature of private credit evolves and expands, there is no assurance that current/historical performance trends (largely favorable) will continue. The solid historical performance of private lending may not be comparable performance as the market grows and as new entrants change focus to non-traditional alternative assets and more challenging and stressed credit environments occur, particularly higher interest rates.~~
  - Enhanced covenant protections and documentation relative to broadly syndicated lending markets.
  - Greater ability for lenders to negotiate transaction-specific terms and monitor borrower performance.
  - Diversification benefits through access to issuers and asset types not available in public markets.
  - Structural protections, including collateralization, overcollateralization, cash flow controls, and other credit enhancements depending on the investment structure.
  - Historical performance in certain private credit segments that has demonstrated recovery characteristics comparable to or stronger than similar public market exposures.

Refer also to guidance published by the NAIC Capital Markets Bureau on private credit and its characteristics.

Note that the Annual Statement includes new disclosures and reporting requirements to improve the identification of different types of private securities. For year-end 2026, insurers will be required to disclose the SEC registration status for each investment: public, Rule 144A, private placements (defined to include Regulation D, Section 4(a)(2) exempt or other exclusion from SEC registration), or not applicable because the investment is not within the scope of the Securities Act of 1933. An aggregate disclosure in Note 5.T—Private Securities to capture key data by each grouping of investments by registration status to allow for ease of regulator review. The reporting will be provided in an electronic column in all investment reporting schedules (held, acquired, disposed) for short-term investments, cash equivalents, issuer credit obligations, asset-backed securities, common stock, preferred stock and other long-term investments.

Fair Value Measurement Hierarchy

An important element in evaluating risks associated with valuation of private investments (equity or credit) is the level of input available to determine fair value. To increase consistency and comparability in fair value measurements and related disclosures, the fair value hierarchy (see SSAP No. 100) prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets (Level 1) and the lowest priority to unobservable inputs (Level 3).

- **Level 1** inputs are quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date.

- **Level 2** inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. Level 2 inputs might include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in inactive markets, or prices derived from inputs that are observable (e.g., interest rates and yield curves).

- **Level 3** inputs are unobservable inputs for the asset. Unobservable inputs are used to measure fair value to the extent that relevant observable inputs are not available. These inputs often involve significant judgment and estimation, including the use of internal models and assumptions.

When reviewing Level 3 assets, analysts should distinguish valuation classification from credit risk assessment. The fair value hierarchy is intended to identify the nature of inputs used to measure fair value, not to assign a credit risk classification. Therefore, a Level 3 classification reflects the use of a significant number of unobservable inputs and should not be interpreted, on its own, as evidence of elevated credit risk. Certain long-duration insurance assets may have limited observable market inputs but still exhibit stable contractual cash flows and strong credit characteristics. In addition, some assets may be classified as Level 3 because observable valuation inputs are not available at the measurement date, and those assets may subsequently migrate to Level 2 once observable inputs become available.

Information associated with fair value measurement is provided in Note 20 (Fair Value Measurements) of the Annual Statement and can assist regulators in assessing the risks associated with an insurer's private investment holdings. In addition, information on fair value hierarchy reported in the investment schedules can be utilized to identify individual securities warranting additional review.

Private Letter Ratings (PLRs)

Privately rated securities reported by U.S. insurance companies have become more prevalent in recent years. The greater use of PLRs is generally consistent with the overall increase in private credit investments by insurers, particularly life companies. PLRs provide proprietary details of investments and are only communicated to the issuer and a specified group of investors. Therefore, these investments do not benefit from the market validation that comes from market transparency (multiple investors, publicly viewable ratings, etc.) and often come as a single rating rather than multiple ratings. The NAIC has required insurance companies to submit PLRs for verification since 2018, whereby the NAIC's SVO reviews that the letter submitted is for the appropriate security and the current year. In addition, effective in 2022, insurers are required to file full rating rationale reports for PLR requests with the SVO, to partially mitigate concerns regarding the lack of transparency of PLRs.

When reviewing securities that have been assigned PLRs, analysts should consider that the growth in PLRs is largely a reflection of increased private market issuance and the continued evolution of private credit markets, rather than, by itself, an indication of deteriorating credit quality. As market activity shifts toward newer private credit asset classes, the use of PLRs may increase because these assets are often issued in private markets and may not be broadly or publicly rated or publicly disseminated. Analysts should also consider the insurer's broader credit assessment framework, including internal underwriting, investment committee review, and ongoing surveillance, as ~~investments in~~ private assets generally do not rely ~~solely~~ on agency ratings for credit evaluation.

Risk assessment procedures should be applied in a manner that distinguishes among:

1. Private placements and other established private fixed income investments;
2. Emerging or more complex private credit strategies, including certain direct lending, feeder funds, privately-rated CLO, and asset-based finance structures; and
3. Investments characterized by valuation uncertainty or limited transparency, including securities primarily reliant on private letter ratings or significant Level 3 valuation inputs.

The presence of a private letter designation rating alone should not be viewed as indicative of elevated risk. Analysts should prioritize review of investments exhibiting multiple risk characteristics, including lower credit quality, limited transparency, valuation complexity, concentrated exposures, or complex structures.

Unfunded Private Equity Commitments

Insurers have continued to expand their allocations to private equity, as evidenced by the increase in unfunded commitment levels in recent years. These funding commitments—contractual obligations to contribute capital to private equity funds over time—have grown along with insurers' appetite for higher-yielding, long-duration assets amid heightened market volatility. This trend underscores a strategic shift toward private markets, although it also introduces additional considerations around liquidity management and possible valuation uncertainty.

Private equity and private credit limited partnership agreements typically include a funding commitment, which may require the limited partners to reserve a significant amount of liquid assets to meet funding calls. Failure to meet a funding call could result in severe penalties. This could significantly impair the insurer's liquidity, as any reserved funds would not be readily available to pay the insurer's other obligations.

Analysts should evaluate whether the insurer has incorporated those commitments into its liquidity planning, cash-flow forecasting, and overall asset-liability management process.

Procedures

- Review Private Security Code details, Note 5.T disclosures, and available analytical tools to identify concentrations in:
  - Complex private credit structures;
  - Securities backed by private letter ratings;
  - Investments with significant Level 3 valuation inputs;
  - Below-investment-grade or unrated private credit exposures; and
  - Asset classes exhibiting elevated complexity, opacity, or valuation uncertainty.
  - When evaluating private placements, analysts should consider credit quality, diversification, and performance characteristics and avoid relying solely on registration status as an indicator of risk
  - Ratio of private securities in aggregate by asset type, and by security code category to total invested assets

~~• Review the Private Security Code details in the investment schedules, and aggregate private securities information in Note 5.T.; or utilize iSite+ tools, to identify a concentration in private securities.~~

  - Ratio of Private securities in aggregate and by security code category to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and to policyholder surplus (P&C)

- Change in private securities from the prior year

- Review the SVO Administrative Symbols provided for the insurer's bond portfolio on Column 6 of Schedule D, or utilize iSite+ tools, to identify a concentration in securities ~~backed by~~ with PLRs (i.e., symbols PL and PLGI).
  - Ratio of securities with PLRs to total invested assets
  - Ratio of securities backed by PLRs to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health) and policyholder surplus (P&C)
  - Change in securities ~~backed by~~ with PLRs from the prior year
- Review information provided in Note 20C of the Annual Statement (Fair Value Measurement) or utilize iSite+ tools, to identify the extent investments (by type of financial instrument) have a fair value determined with unobservable inputs (i.e., Level 3 inputs).
  - Ratio of Level 3 or Level 2D securities in aggregate to total invested assets
  - Ratio of Level 3 or Level 2D securities to capital and surplus plus AVR (Life/A&H), to capital and surplus (Health), and policyholder surplus (P&C)
  - Change in Level 3 or Level 2D securities from the prior year
- Utilize information on fair value hierarchy reported in the investment schedules to identify individual securities warranting additional review.
- Review Note 14 – Liabilities, Contingencies, and Assessments, to assess the insurer's exposure to unfunded commitments.

- Review Schedule BA Part 1, Column 19 total—Commitment for Additional Investment, as a percentage of Policyholders' Surplus, to assess the magnitude of the impact of unfunded commitments on the insurer's valuation.

Additional Review Considerations

- For insurers with a concentration in bonds with PLRs:
  - ~~Request the support of the NAIC's Securities Valuation Office (SVO) to investigate the rating sources for the securities (with a focus on concentrations with any one rating agency and/or securities with only one rating) and consider the potential impact on the insurer's RBC charges and investment risk exposures.~~
  - Request details from the company on its own internal ratings for securities ~~backed by~~ with PLRs where applicable and compare with rating agency rating for discrepancies.
- For insurers with a significant concentration in Level 3 securities, consider reviewing the investment schedule detail to identify whether the investments with Level 3 fair values are private, whether a private letter rating is the source of the NAIC designation for these items, and the extent the investments have aggregate deferred interest or paid-in-kind (PIK) interest.
- Consider requesting additional information on the ongoing performance of these assets and/or the pricing assumptions and methodologies used in fair value measurement.
- If exposure to unfunded commitments is significant, consider whether the insurer's management and board have a clear understanding of differences in liquidity and market value drivers, as well as the reasons for different yield and cash-flow characteristics, as unfunded commitments contractually obligate the insurer to contribute capital to private equity funds over a designated period of time.
- If necessary, consider utilizing an investment specialist to assist in asset valuation considerations.
- ~~If appropriate, consult with or request an Opinion from the NAIC's SVO or Structured Securities Group (SSG) on a specific investment holding or transaction. [A state insurance regulator can ask for SVO or SSG analytical~~

~~assistance with respect to any investment related activity or in connection with an assessment of investment-related aspects of a Regulatory Transaction (defined in the P&P Manual). The department can direct an insurance company to file relevant information with the SVO or SSG for the purpose of that analysis and the SVO or SSG will issue a report back to the department.]~~

- Request a Preliminary Analysis from the NAIC's Capital Markets Bureau (CMB) to assess the insurer's overall portfolio investment risk exposures and suggest additional follow-up procedures that can be performed by the department to address overall portfolio issues identified. Request analytical assistance from the CMB to better understand and measure the investment risks related to a particular asset class, investment-related activity, or market trend.

----------Detail Eliminated to Conserve Space----------

Invested Asset Exposure to Climate Change, Transition and Asset Devaluation Risk

Identify and assess the potential exposure of the insurer's investment portfolio to the impact of material climate change and/or energy transition risks. The insurer's investment portfolio may be subject to prospective devaluation of the assets/changes in the asset return associated with its holdings of climate-affected assets. Transition risks refer to stresses on certain investment holdings arising from the shifts in policy, consumer and business sentiment, or technologies associated with the changes necessary to limit climate change. A few examples of investment holdings and sectors generally subject to greater levels of transition risk include oil/gas, transportation, heavy manufacturing, and agriculture. In assessing an insurer's exposure to these risks, review information disclosed by the insurer in its responses to the NAIC's Climate Risk Disclosure Survey, U.S. Securities and Exchange Commission (SEC) filings, and/or the Own Risk and Solvency Assessment (ORSA) Summary Report filings. In addition, review the results of basic scenario analysis conducted by the NAIC using insurers' Annual Statement filings (U.S. Insurance Industry Climate Affected Investment Analysis) to identify potential concentrations in exposure.

Procedures

- Review information provided in the insurer's response to the NAIC's Climate Risk and Disclosure Survey (if available) on its exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review relevant information provided in the Own Risk and Solvency Assessment (ORSA) Summary Report, and/or U.S. Securities and Exchange Commission (SEC) 10-K or 10-Q filings (if available) that discusses the insurer's exposure to material climate change/energy transition risk and related mitigation activity in this area.
- Review information provided in the NAIC's U.S. Insurance Industry Climate Affected Investment Analysis to identify potential concentrations in insurer exposure.
- Review the Climate Affected Assets Dashboard to assess an insurer's exposure to assets that might be subject to transition risk in the coming years. The dashboard allows the user to view an individual insurer's investment portfolio as of year-end, which has been classified into buckets of climate affected assets (i.e., Fossil Fuel, Energy Intensive), with the ability to view those categories as a percentage of the overall portfolio. Companies that do not have assets subject to transition risk (i.e., Treasuries, Cash) will not be included.

Additional Review Considerations

- Review the insurer's investment policies and strategies to assess whether material climate change, transition and asset devaluation risk considerations have been appropriately implemented into the company's investment processes.
- Review the most recent examination report and summary review memorandum (SRM) for any findings regarding climate change/energy transition risks.
- If concerns exist, consider requesting information from the insurer regarding how the insurer manages its exposure to material climate change/energy transition risk, including how it identifies and estimates current and prospective exposures and the limits (if any) in place to avoid concentrations.

----------Detail Removed to Conserve Space----------

ANNUAL CREDIT RISK ASSESSMENT

----------Detail Removed to Conserve Space----------

Credit Quality and Appropriateness of Asset Intensive Reinsurance Placed Through Modco or FWH Agreements (Life/A&H Insurers)

Modified Coinsurance and Funds Withheld Agreements

Concerns may exist regarding the quality, adequacy and appropriateness of assets held to support asset intensive reinsurance placed through Modified Coinsurance (Modco) or Funds Withheld (FWH) agreements, particularly as investments become increasingly complex. Concerns may include controls and governance over investment practices, valuation and ratings of assets, and if material amounts of assets involve related party transactions.

Where collateral held is related to Modco and FWH reinsurance, the analyst should review the information in Note to the Financials #5L(1), #5L(4) and #5L(5), and Schedule S—Part 8—Reinsurance Agreements with Funds Withheld and Modified Coinsurance, in conjunction with other credit, operational and strategic risk of the insurer's reinsurance program. Additionally, review the analysis considerations related reserve reporting required by AG 53 (complex assets) and AG 55 (assets supporting reinsurance) outlined in the Reserving Risk Assessment and SOA procedures and guidance.

Where the company is engaged in material Modco and FWH arrangements, the analyst can use the detail of collateral received and held under Note 5L(4) to identify the types of assets held by investment schedule, and gain an understanding of the materiality of aggregate BACV of the collateral received to the insurer's asset portfolio. Further, the Note #5L(5) disclosure identifies if securities held as collateral under Modco or FWH agreements are also pledged under other arrangements, in which case they would not be for the benefit of the reinsurer or available to fulfill the liabilities of the reinsurance contract. The analyst can use the information in Schedule S—Part 8 to identify any concerns with the types of assets and credit quality of assets held under ceded or assumed Modco or FWH agreements.

Procedures / Data

- Identify the types of reinsurance agreements and jurisdiction of the reinsurer [Annual Financial Statement, Schedule S – Part 3] and determine if concerns may exist over the adequacy and quality of assets held by reinsurers in support of ceded reserves that may require further analysis or inquiry to the insurer.
    - Compare the BACV of the collateral received and assets held under Modco/FWH Reinsurance Agreements to the recognized obligation for Modco and FWH assets. [Annual Financial Statement, Notes to the Financials #5L(4)(m and n)].
    - Identify if investments held under FWH agreements (including Modco) are related to the Modco/FWH reinsurer [Annual Financial Statement, Notes to the Financials 5L(5)(o-v)].
    - Identify if the insurer is engaged in ceding business under Modco and FWH agreements with offshore reinsurers.
        - Gain an understanding, through review of Schedule S - Part 3, of the types of insurance business ceded, the reinsurer's jurisdiction, if affiliated or non-affiliated, and applicable collateral requirements by type of reinsurer (i.e. authorized, unauthorized, reciprocal jurisdiction, certified). See the following sections for additional procedures for assessing risk for offshore unauthorized reinsurance.

- Review Schedule S – Part 8 to determine if concerns exist regarding the types of assets held or the credit quality of assets held under Modco/FWH agreements. Consider if the aggregate of medium or lower quality assets held represent a material amount of the related Modco/FWH liabilities.
  - Review Schedule S – Part 8 in comparison to Life RBC (asset schedules) to ensure asset subtotals match. If differences exist, inquire of the insurer, as differences may have an impact on the RBC calculation.
- Determine if assets held under Modco or FWH agreements are also pledged under other agreements [Annual Financial Statement, Notes to the Financials #5L(5)].

Additional Review Considerations

- If concerns exist regarding the types of assets held or the credit quality of assets held under Modco or FWH agreements, or concerns over reinsurance reporting, inquire of the insurer to:
  - Identify the applicable reinsurers and reinsurance agreements. Annual Financial Statement, Schedule S – Part 3, Financial Profile, Reinsurance Dashboard]
  - Has the insurer entered into new offshore unaffiliated Modco or FWH agreements for which the agreement was not required to be reviewed by the Department?
  - If offshore reinsurance, gain an understanding of the types of business ceded and the insurer's business purpose for ceding the business offshore.
  - Gain an understanding of the collateral requirements for the type of reinsurance and jurisdiction.
  - Request a copy of the applicable Modco/FWH reinsurance agreements and assess if the investment requirements are in compliance with the terms of the agreement and the state's reinsurance statutes.
  - Gain an understanding of the insurer's investment practices, who is managing the investments supporting the reserves, governance policies and use of asset managers for reinsurance assets.
  - If the management of the assets withheld or placed in trust in support of the reinsurance agreement is transferred to the reinsurer or an asset manager:
    - Assess the degree to which the ceding company has provided direction and oversight to the reinsurer in terms of investment guidelines and limitations.
    - Closely monitor the assets in the funds withheld or trust account to verify they are in compliance with state laws and ceding company guidelines, and identify concentrations in complex or risky investments.
- If a material amount of assets held under Modco or FWH agreements are also pledged under other arrangements, inquire of the insurer to gain a better understanding of their use of collateral assets within their reinsurance program and to ensure the insurer is in compliance with collateral requirements.
- Refer significant concerns identified to the examiner for further review, if warranted.

Jurisdictional Risk Considerations

Additional concerns may exist when asset intensive reinsurance is placed with ~~unauthorized~~ reinsurers from ~~offshore~~ jurisdictions with varying regulatory requirements and oversight. The purpose of the following is to assist the analyst in evaluating the insurer's exposure to significant reinsurance arrangements ceded to reinsurers domiciled in certain jurisdictions presenting additional jurisdictional, transparency, capital, reserving, or collateral-related risks, consider the following additional review considerations.

Specific Risks

In recent years, regulators have observed a rise in the use of offshore reinsurance transactions (both affiliated and unaffiliated) to unauthorized reinsurers in these jurisdictions. An underlying concern is that this activity could result in reduced policyholder protection or regulatory arbitrage, and rising reinsurance credit risk, if reinsurance reserves or the underlying collateral supporting those ceded reserves is not sufficient, all of which should be carefully assessed and monitored. Some additional considerations are provided below including an optional "reinsurance comparison worksheet" that can be used to compare different accounting, reserving and capital standards across jurisdictions. In certain international jurisdictions regulators have had difficulties determining if offshore reinsurance arrangements are affiliated or unaffiliated as information about the ownership of the reinsurer may not always be readily available or easily obtained, therefore it is important to have good communication with cedents and relevant foreign jurisdiction regulatory authorities.

A potential concern with utilizing unaffiliated third-party offshore unauthorized reinsurance is when management of the assets withheld or placed in trust in support of the agreement is transferred to the reinsurer or an asset management affiliate, which may be the case in some asset intensive reinsurance arrangements. In these situations, the reinsurer may have incentive to reallocate the portfolio into more complex assets to achieve a higher rate of return, including assets originated by or placed within its affiliated entities.

Finally, while historically more common in property/casualty insurance, there have been recent indications that more reinsurance sidecars are being formed in the life/annuity reinsurance industry. Sidecars are limited purpose reinsurance transactions where third-party investors infuse capital in exchange for dividends, and may also provide other services, such as asset management services in exchange for fees. The purpose is to offer alternative capital to reduce volatility in earnings and capital of the ceding insurers. Since sidecars arrangements may be formed with different strategies and interests in mind (infuse capital support, specialized asset management expertise, favorable offshore capital/tax treatment, reduce volatility, etc.), it is important to understand the structure of the sidecar deal, and whether the ceding insurance company has sufficient governance and controls over services provided by the sidecar.

Procedures / Data (Apply based on jurisdictional concerns.)

- Identify the type(s) of reinsurance agreements, type(s) of business ceded, and jurisdiction(s) of the unauthorized offshore reinsurer(s). Determine if amounts ceded to unauthorized offshore reinsurers are material. [Annual Financial Statement, Schedule S – Part 3; Financial Profile; Reinsurance Dashboard]

Additional Review Considerations (Apply based on jurisdictional concerns.)

- For material new reinsurance transactions placed with unauthorized offshore reinsurers, regulators should gain an understanding of the business purpose for the transaction.
- Monitor the reinsurer's credit and financial strength ratings.
- Consider utilizing the Reinsurance Comparison Worksheet developed by the Macroprudential (E) Working Group to assist in understanding and evaluating cross-border reinsurance treaties where different regulatory systems are involved.
- Gain an understanding of the regulatory requirements for assets held to support the reinsurance agreement.
- Assess the credit quality and liquidity of the funds-withheld assets supporting the agreement, including assessing risks associated with complex assets backing the reinsurance agreements. [e.g. for Life/A&H: Review of Actuarial Guideline 55 filing, if required; Annual Statement Note 5; Schedule S, Part 8 for Life/A&H]. Refer to additional Modco/FWH procedures above.

- For assets managed by third-party reinsurers or asset managers (i.e., funds withheld or held in trust), closely review the assets to identify relationships with the reinsurer and ensure compliance with ceding company guidelines and state investment laws (i.e., single issuer limitations).
- Consider engaging with foreign jurisdiction regulatory authorities to understand their applicable capital, investment, and reserving requirements as well as their understanding of the ownership structure of the reinsurer and the regulatory agency's supervisory plan for the reinsurer.
- Review information provided in the insurer's Actuarial Guideline 55 filing, if required, relating to asset adequacy analysis, reserves and assets supporting asset intensive reinsurance transactions, if applicable. (See additional guidance in the Life Reserve Risk chapter, III.B.8.b.ii)
  - Coordinate with the Valuation Analysis (E) Working Group, as appropriate, to access information from their targeted review of AG-55 filings and/or request additional support.
- Consider requesting information from the cedent, the reinsurer, or the reinsurer's domiciliary regulatory authority, for the Department's ongoing risk assessment. The level of detailed information requested may be dependent on the materiality and complexity of the transaction as well as the assessed likelihood and potential severity of loss due to default, after considering collateral, controls, and other mitigating factors. For example:
  - Reporting on the reinsurer (noting that other jurisdictions may have disclosure limitations). Examples include:
    - Financial condition of the reinsurer quarterly,
      i. For Example: include RBC calculations for the entity under the fully compliant U.S. statutory basis and ~~foreign jurisdiction's approach~~under its domestic regulatory accounting requirements.
    - Audited financial statements of the reinsurer.
    - Unaudited statements of the reinsurer (if possible, prepared under US GAAP and GAAS) and supplemental notes that provide detail on reserves/ capital, investments, and reinsurance activities.
    - Reinsurer's standalone cash flow testing results/memorandum, actuarial valuation report.
    - Assets supporting the ceded business and asset adequacy testing that the reinsurer provides to their foreign regulatory authority.
    - The foreign regulatory authority's examination or inspection report of the reinsurer.
  - Reporting on the cedent in addition to statutory filing requirements (to the extent that it is not duplicative), such as:
    - Actuarial Opinion and the supporting Memorandum annually, as well as reporting of mortality and policyholder behavior experience development vs. pricing expectations
    - Regular summary reporting of all transactions, or other material blocks of business ceded (e.g. annual in conjunction with AG55 requirements).
  - Reporting on the transaction, specifically, noting that in unaffiliated transactions the cedant may not be aware of all of the aspects of the reinsurer's business plan or global risk management strategy and may not be able to compel their disclosure if they are not contractually required.
    - Gain an understanding of the operating results of the entire reinsurance structure from the perspective of each party involved, (i.e., cedent, reinsurer/retrocessionaire, unauthorized offshore reinsurer), noting constraints on availability referenced above
    - Confirm if the transaction is subject to AG55 reporting
    - Consider requesting projections of all material components of the reinsurance structure if not subject to AG55, with focus on impact to the cedant

EXAMPLES OF REPORTING REQUESTS:

~~The following is an example of a detailed business plan request:~~ *The following provisions are examples only, may not be applicable in every situation and are not intended to establish standardized requirements, minimum thresholds regulatory safe harbors. Each provision should be considered individually, as appropriate.*

1. Request an updated business plan including the business purpose, investment guidelines associated with the reinsurance structure ~~policy~~, and quarterly projections for operations of the entire reinsurance structure, including projection of all pertinent aspects of the business ceded from the perspectives of all entities in the reinsurance structure.
    - Three projections, each for twenty years, as the risk flows from entity to entity.
        - One is a level equity and interest projection to represent a baseline expectation.
        - Two projections from the 1000 stochastic projections developed as part of the quarterly reserve and capital calculation. The two projections represent the 15th and 5th worst ending surplus positions and are intended to approximate moderately adverse and minimum capital level projections.
    - The projections provide,
        - Broadly, product/treaty level detail as well as the aggregated cash flows. Annual projected amounts for reserves, capital, net after tax income, capital transfers among the entities within the system, and cedent RBC, among many other variables are provided for the system.
        - Present value of projected capital contributions from cedent to the reinsurers for each scenario.
        - Cedent's starting statutory reserve and details the ceded and assumed amounts throughout the system, giving insight into the amount of reserve and

- If the agreement was approved by the Department, assess the compliance with the terms and conditions of any MOU, contractual agreement or conditions placed on the approval of the transaction.
- Conduct periodic in-depth meetings with the cedent's senior management where agenda items may include:
    - Financial/operating results for all material entities in the reinsurance structure on a U.S. statutory basis and pro-forma RBC, where relevant and available
    - Relevant initiatives and filings
    - Investment reporting on the assets supporting the agreement including investment income results, rebalancing, and monitoring
    - New sales reporting, and other supplemental information that is relevant to the block of business ceded
    - Compliance with pre-approval conditions
- For the next scheduled examination, recommend the examiner verify the funds-held assets associated with foreign reinsurers to ensure existence, accuracy, and admissibility; and review of the reinsurance agreements for proper risk transfer.

Yellow Highlights – Changes recommended by Commentors that Staff supports accepting after 1st Exposure.
Grey Highlights – Edits recommended by Staff after 1st Exposure.
Blue Highlights – Edits recommended following 2nd Exposure.

Special Notes:

The following procedures do not supersede state regulation but are merely additional guidance analysts may consider useful only if the state has adopted the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450).

Form D – Prior Notice of a Transaction

Form D is transaction specific and is not part of the regular annual/quarterly analysis process. The review of these transactions may vary as some states may have regulations that differ for Form D.

----------Detail Removed to Conserve Space----------

Assessment of Form D – Asset Intensive Reinsurance Transactions Placed Through Modco or FWH Agreements (Life/A&H Insurers) ~~with Unauthorized/Offshore Reinsurers in Offshore Jurisdictions~~

The purpose of the following is to assist the analyst in evaluating the significant reinsurance arrangements ceded to reinsurers domiciled in certain jurisdictions presenting additional jurisdictional, transparency, capital, reserving, or collateral-related risks.

Best Practices for Review of the Agreement:
Reinsurance transactions with unauthorized reinsurers in foreign/offshore jurisdictions ~~that are unauthorized and~~ (not reciprocal or certified reinsurers), may be based on capital and reserving standards that vary materially from U.S. standards. Therefore, it is important when reviewing these transactions to understand the foreign jurisdiction's regulatory framework and the financial impacts of the transaction.

In addition to the procedures described above for Form D review, consider the following best practices for review, and pre-/post-approval considerations, of ceded reinsurance transactions with unauthorized reinsurers in offshore jurisdictions.

Coordination with other regulatory agencies should be prioritized where possible to ensure consistent and risk-aware guidance from all regulators. The best practices listed below are context dependent. Input from the reinsurer's domestic regulator may be helpful in determining what guardrails are most prudent.

To support an effective and efficient review, regulators may consider focusing initially on the most relevant information and expanding the scope of analysis where preliminary findings suggest additional review would be beneficial.

Note: While some of the following best practices may be relevant and useful for any unauthorized offshore reinsurance agreement, the following are intended primarily for ~~life~~ asset intensive life reinsurance agreements, and should be applied based on jurisdictional concerns.

Analytical Tools and Practices

1. Assess the companies' governance and controls to monitor and mitigate risks such as reinsurer credit risk; identify information that can be obtained from companies' existing processes as well as potential blind spots.
2. Request information to complete the review. See the example. ~~such as:~~

EXAMPLES OF INFORMATION REQUESTS

~~*The following is an example of items to consider include in a request for information:*~~
The following provisions are examples only, may not be applicable in every situation and are not intended to establish standardized requirements, minimum thresholds regulatory safe harbors. Each provision should be considered individually, as appropriate.

a. A business plan that includes the business purpose of the transaction, and projections including a three-year proforma financial statements and RBC for the insurer and the reinsurer.
    i. For the reinsurer, recommend amounts be reported not only in the framework that will be reported to the reinsurer's foreign regulatory authority but also request, at a minimum, a balance sheet and income statement for the reinsurer using U.S. GAAP presentation and U.S. Statutory presentation.
b. All licensing and other relevant transaction documents (e.g. master transaction agreement, reinsurance agreement, supplemental trust agreement, related investment management agreement, etc.)

3. Utilize the Macroeconomic Working Group Reinsurance Worksheet, where appropriate. Note that Worksheet's may need to be modified and customized accordingly, for example, to work with funds withheld agreements, or where the U.S. state insurance regulator is imposing specific requirements, in particular requirements based on US RBC .
4. Transactions should undergo review by both the analyst and supervisor and based on complexity, may also undergo an additional supervisory review.
5. Communication and Coordination with the entities during the review process, for example:
    a. In-person meetings with the Company for transaction walkthroughs and initial discussions
    b. Weekly standing meetings with both the Company and the actuarial or other specialists assisting on the review.
6. Communicate with the unauthorized reinsurer's regulatory authority to discuss the transaction, gain an understanding of the foreign jurisdiction regulator's oversight and any concerns with the reinsurer.
7. Retain an actuarial specialist and/or an investment specialist to assist in the review of the transaction.
8. Perform an independent review conducted by a senior analyst in conjunction with a separate review performed by the specialists.

Analysis Procedures, in addition to general Form D procedures outlined above:

9. Perform a detailed review of all legal agreements.
    a. Assess if the transaction meets the requirements of the state's Holding Company Systems statute, for example arms-length terms and provisions.
    b. Does the transaction contain appropriate contractual protections against counterparty credit risk including, for example, collateral and recapture terms; and dividend restrictions?
10. Review the investment guidelines.
    a. Do they define the asset classes eligible for the FWA/ the credit quality, duration, and concentration limits, with sub-limits by instrument and class?

b. Confirm that the management of the assets supporting the transaction are aligned with the cedent's investment policies and guidelines. Where not, identify reasons for the difference and assess the materiality and potential impact.
c. Review the investment and custody rules. Does the investment management agreement subject the manager to the policies established without authority to withdraw or transfer the assets? For funds withheld and modified coinsurance agreements, do the custody and title remain exclusively with the cedent?

11. Gain an understanding of the accounting framework being used by performing a detailed actuarial review of material items:
    a. ~~Any alternative reserve methodology and plan of operations of the reinsurer~~ The reserve methodology (including if different from U.S. reserving standards), the plan of operations of the reinsurer, or changes in those plans, relevant to the the transaction.
    b. Pre-reinsurance vs post-reinsurance balance sheets, ceding commissions
    c. A comparison of the reserve and capital requirements for onshore vs offshore
    d. Recapture provisions
    e. Investment guidelines
    f. Company's standalone cash flow testing
2. Gain an understanding of any reinsurance collectability concerns
12. Perform a detailed review of the Company's risk transfer analysis to identify any terms that highlight concern or that could limit risk transfer. Determine if the agreement transfers risk.
13. Perform a limited-scope examination, if determined necessary, over standalone asset adequacy testing
14. Assess the effectiveness of the cedent's counterparty risk mitigation, noting that different reinsurance structures may require different solutions (for example, if assets are in a trust or not). Gain an understanding of the basis for managing the solvency of the reinsurer.

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EXAMPLES OF REINSURANCE AGREEMENT TERMS:

~~*The following is an example of terms of an agreement that were intended to help mitigate financial risk of failure:*~~ *The following provisions are examples only, may not be applicable in every situation and are not intended to establish standardized requirements, minimum thresholds regulatory safe harbors. Each provision should be considered individually, as appropriate.*

a. *100% Quota Share Coinsurance w/ Funds Withheld* Coinsurance or Modified Coinsurance in place of ordinary coinsurance
b. *Assets with Book Value equal to 100% of U.S. Statutory Reserves retained on cedent's balance sheet.*
c. *Supplemental Trust with additional assets equal to 5% of U.S. Statutory Reserves are required to be held in a supplemental trust as overcollateralization with a US bank as Trustee.*
d. *Granular negotiated investment guidelines subject to state insurance department approval– i.e., failure to retain RBC ratio triggers more conservative investment guidelines.*
e. *Market-to-Book* Restrictions: Limitations or conditions on collateral assets when the market value of such assets is less than *85% of book value of those assets.*
f. *Excess collateral may not be withdrawn by reinsurer if RBC ratio is less than 250% CAL (500% ACL), calculated on a fully compliant U.S. statutory basis, or if the Market Value of collateral assets is less than 90% of book value.*
g. *Reinsurer cannot pay dividends if RBC ratio is less than 250% CAL (500% ACL) calculated on a fully compliant U.S. statutory basis.*
h. *Parental Guarantee*
i. ~~*Cedent can elect to*~~ *Recapture permitted if the reinsurer's RBC ratio falls below 200% CAL (400% ACL) or if the reinsurer fails to pay any amount due, including topping up the collateral accounts. If collateral fell to a specified percentage, such as 105%, and the reinsurer fails to top off, the cedent can recapture with full access to all 105% of statutory reserves in collateral.*
i. *Two layers of collateral: The funds withheld ~~trust~~ account must be equivalent to 100% of the*

15. Assess the settlement mechanics. Is the settlement a cash settlement? Does it include a reconciliation of required reserves vs. the funds withheld asset balance with scheduled top-off, and top off of the Trust Account to a specified level?
16. Assess the termination and recapture triggers. Does the agreement provide for the cedent's right of recapture upon a reinsurer's insolvency event, capital (e.g., RBC) Level, and provides for a notification trigger upon the capital ratio (e.g., RBC) falling below a specified level, e.g. 300% RBC.

Best Practices for Pre-Approval of the Transaction

Consider entering into a Memorandum of Understanding (MOU) or similar contractual agreement, or require conditions as part of the final approval of the transaction MOUs. The terms of the MOU between the cedent and the insurance department or conditions for approval could include reporting, notification and capital requirements. For example:

EXAMPLES OF POSSIBLE TERMS FOR AN MOU:

~~*The following example of terms a Memoradum of Understanding as part of approval of the transaction.*~~ *The following provisions are examples only, may not be applicable in every situation and are not intended to establish standardized requirements, minimum thresholds regulatory safe harbors. Each provision should be considered individually, as appropriate.*

1. For Modco and Funds Withheld agreements the cedent retains at all times the legal title and custody of the assets. ~~of the Funds Withheld Account (or Trust account)~~ For collateral held in trust, the assets are held in the name of the trustee.
    a. Funds withheld assets are held in a Trust where cedent is grantor and reinsurer is beneficiary. All assets are held on cedent's balance sheet in a segregated custody account in US banks.
    b. Investments held in the Funds Withheld Account account shall be in the name of the cedent.
    c. Custody is operated through a qualified custodian.
2. Funds Withheld Account or Trust account is established at, for example, 5% over the required statutory resources, where the Trust is voluntary contractual collateral, i.e. security, not for reinsurance credit.
3. Consider basing the terms of the agreement ~~Require the terms of the agreement to be based~~ on fully compliant U.S. Statutory Reserves and RBC, irrespective of how the foreign regulatory authority monitors solvency.
4. Consider ~~Require~~ restrictions on dividend and capital distributions without first obtaining Department approval.
    a. For example, the reinsurer cannot pay dividends within its first year. Subsequently it cannot pay dividends that will cause its RBC ratio to fall below, for example, 350% CAL RBC.
    b. For example, the cedant cannot pay dividends should its CAL RBC ratio fall below a sliding scale, for example, that starts at 400% and ends at 350% over 8 years. Any ordinary or extraordinary dividends require Department approval for the first three years after the transaction closes.
5. Consider requiring notification to the Department, such as for future or contemplated affiliated and non-affiliated reinsurance transactions, qualified financial contracts
6. ~~Require~~ Consider parental guarantees or keep-well agreements assuring the parent will provide capital support to maintain a certain RBC level or to ensure claims payments.
7. To the extent not already required by AG55, consider to monitor mortality and policyholder behavior experience, actual vs. expected, consider requiring on an annual basis, the cedent perform Asset Adequacy Testing for the ceded policies, under the same requirements and moderately adverse scenarios and using the same assumptions it uses for Asset Adequacy Testing generally, but on a stand-alone basis for the business subject to reinsurance. The results of the stand-alone Asset Adequacy Testing, including a summary of the analysis, assumptions, and results, would be submitted to the department as a separate opinion of the Appointed Actuary, concurrently with the filing of the annual Actuarial Opinion. To the extent that the funds withheld assets, exclusive of any Letters of Credit, are insufficient to satisfy all cash flows under such analysis, the cedent could be required to establish additional reserves ~~will be established at the cedent~~ accordingly. the cedent will submit to the department a separate opinion of the Appointed Actuary, summarizing the analysis, assumptions, and results of the stand-alone Asset Adequacy Testing.

EXAMPLES OF TERMS OF MOU, continued:

a. On an annual basis the cedent would ~~will~~ report on mortality experience, including expected to actual, along with any changes in mortality assumptions used in establishing reserves.
b. The Cedent would ~~will~~ make submissions to the Department for prior approval for additional cessions on an ongoing basis.
c. The Cedent would ~~will~~ report a quarterly summary of transactions to date on a level of detail as requested by the Department.
d. Targeted restrictions (for example, taking into consideration the location of the assets) on retrocessions without the prior approval of the department could be established to ensure that assets remain available to meet policyholder obligations, or for other purposes as specified by the Department. Any violation of this restriction ~~will~~ would result in the automatic retraction of the Department's approval.
e. Failure to comply with these conditions ~~will~~ would result in retraction of the Department's approval.

8. Where there are material differences in regulatory standards and reasonable approximations can't be developed, consider requiring ongoing reporting whereby the foreign reinsurer provides annual financial statements and CAL RBC ratio with reserves and capital including asset adequacy testing and RBC, in accordance with U.S. Statutory accounting, and U.S. RBC standards.
9. Require AG-55 Reporting or some subset thereof.
10. Quarterly reporting requirements for all entities in the reinsurance structure.
    a. "Reinsurance structure" in this best practice refers to the cedent, any reinsurer/retrocessionaire(s) in the middle, and the offshore unauthorized reinsurer, for a specific block of business.
    b. Capital ratio reporting for all entities in the reinsurance system, for example, X% capital ratio. This requirement is a minimum threshold set by the Department to act as a regulatory backstop to apply a consistent lens across the various regulatory regimes
    c. This quarterly reporting is intended to allow the Department to proactively identify capital adequacy trends or declines in RBC, and take appropriate regulatory action, well before reaching the 300% minimum. Consider requiring similar thresholds for recapture triggers or other risk-mitigating solutions in the reinsurance contract.
    d. Minimum RBC requirement for all entities in the reinsurance system, for example, CAL RBC 300%. The RBC requirement is a minimum threshold set by the Department to act as a regulatory backstop to apply a consistent RBC lens across the various regulatory regimes.
11. In addition to quarterly financial statements and RBC of the reinsurer, request the cedent provide quarterly and annual information detailing various aspects of the treaties, including:
    a. Asset-liability management data
    b. Investment guidelines compliance report
    c. Reinsurer's actuarial report
    d. Reinsurer's audited financial statements
    e. Peer review report on the work of the appointed actuary
    f. Summary of settlement activity
    g. Internal capital calculations

Post-Transaction Ongoing Monitoring – Analysis or Examination

After closing the transaction and during future ongoing monitoring, the analysis should focus on assessing the financial solvency of the reinsurer as well as the cedent, compliance with any terms or conditions of the approval and assessing the ongoing reserve adequacy, credit quality of supporting assets, counterparty risk, and risk mitigating strategies. See guidance and procedures in the Credit Risk and Life Reserve Risk chapters III.B.1 and III.B.8.ii. for Credit Quality, Adequacy and Appropriateness of Assets Held for Modco or FWH Agreements and Actuarial Guideline-55 review.