

***John Petchler,*** *President,* ***on behalf of the PPiA Board of Directors***

December 15, 2020

Mr. Dale Bruggeman, Chair

Ms. Carrie Mears, Vice-chair

NAIC Statutory Accounting Principles (E) Working Group (“SAPWG”)

1100 Walnut Street

Suite 1500

Kansas City, MO 64106-2197

Dear Mr. Bruggeman and Ms. Mears:

The Board of Directors of the Private Placement Investors Association (“PPiA”) appreciates the opportunity to provide comment on “INT 20-10: Reporting Nonconforming Credit Tenant Loans.” Such investments are held by many of our 55 member companies, most of whom are US-domiciled insurance companies that invest regularly in the private placement debt market, including in Credit Tenant Loans (“CTLs”).

The PPiA understands that this exposure is an interpretation of discussion from a mid-November SAPWG meeting and resulted from NAIC Staff’s and Regulators’ desire to work with insurers to find a temporary solution for reporting non-conforming CTLs and to possibly provide capital relief. We know that the NAIC has been in multi-year discussions with Industry regarding these securities, and we appreciate your genuine willingness to accommodate insurers’ needs and look for a mutually agreeable solution. That said, we do have two concerns around the non-conforming CTL proposal which we will detail below. We would also like to offer a solution which we believe would help alleviate both concerns and help move the process forward.

**Timing**

The interpretation requires insurers who have previously been carrying non-conforming CTLs on Schedule D-1 to file all of these securities with the SVO immediately, so that the SVO can review and decide whether to assign an NAIC designation to such securities on or before March 1, 2021. This timing is challenging, as it results in a major reporting change and significant new filing requirements for insurers right before year-end. It also places a significant burden on the SVO staff to review and attempt to assign designations to such securities in a short time window.

The PPiA has begun telegraphing these new rules to our member companies; however, the change has resulted in multiple questions and a lot of confusion around which deals need to be filed, what is required to be filed as supporting documentation, the timing of such filings, whether the ruling was intended to be prospective or retrospective, and what criteria the SVO will use to assign designations to these investments. Given the nature and volume of questions, we expect that there will be a variety of inconsistent responses from insurers at year-end, with some complying fully with the new proposal, some complying partially but perhaps without a full understanding of which CTLs are necessary to file, and some not even aware of the new requirements. The fact that certain insurers will be allowed to continue carrying these securities on Schedule B or BA, while others must file for Schedule D-1 treatment and then hold on Schedule BA, if the SVO cannot assign a designation for any reason, only adds to this confusion.

Other challenges include assembling the documents needed to support the filings. Some of these securities have been on insurers’ books for 15+ years, and insurers may not have documentation stored electronically, such that it’s easy to upload requirements into the NAIC’s systems. In these situations, insurers are forced to retrieve documents from off-site paper storage warehouses, which takes time and reduces the likelihood that such filings can be submitted before year-end. This issue is exacerbated by the current work-from-home conditions under which most insurers are still operating.

The PPiA is also concerned that this will be a first-time filing for many of these securities, and that the requested list of supporting documents for such filings is extensive. (For example, once such transaction that the PPiA is currently aware of has a closing documents package from outside counsel that is 256MB and cannot be sent over email—instead, investors must access these files from an electronic DropBox.) While the PPiA appreciates the SVO’s effort to try and review as many of these transactions as possible between now and March 1st, as a practical matter, we believe it will be extremely difficult for the SVO Staff to review most of these investments and assign designations in this short timeframe. The fact that the SVO currently has no rating methodology criteria in place to assess the risks associated with these securities compounds the difficulties. The PPiA is concerned that the SVO will either not be able to review many of these securities in the allotted timeframe, or that the SVO will be unable to designate such securities without some pre-existing rating methodology in place, and many of these deals will be relegated to Schedule BA reporting with onerous capital treatment (see RBC concerns below).

For the reasons stated above, the PPiA believes it would be best to delay implementation of the new rules from year-end 2020 into 2021. Industry is willing to begin filing all non-conforming CTLs with the SVO to provide transparency for Regulators, and we are willing to work with the SVO to discuss and develop a potential ratings framework in early 2021, so that many of these securities could be designated over the course of the full year. However, we believe that it is too late in the year to adopt new reporting requirements that could potentially have negative capital consequences for insurers, and we think that more time would allow a more thoughtful approach to review such securities and implement the new rules smoothly. As such, we would ask Regulators to consider delaying the reporting and RBC requirements change until year-end 2021. However, if Regulators are unwilling to delay implementation of such rules changes, then the PPiA would ask for relief on the RBC requirement as noted below.

**RBC Requirements**

As discussed above, the PPiA believes that these new interim rules will result in many of the non-conforming CTL transactions moving to Schedule BA, either because the SVO lacks sufficient time to review the investments, or because the SVO is unable to assign a designation without a pre-defined ratings methodology framework. The PPiA’s interpretation of INT 20-10 is that such securities, if reported on Schedule BA, would be assessed a 30% C1 RBC charge. This capital charge is typically assigned to equity securities and limited partnership investments and seems overly conservative for securities which are—at worst—mortgages with a 20-year fixed-income cash flow payment stream derived from an investment grade tenant(s). We note that the current discussions around non-conforming CTLs originated from a desire to provide capital relief for these securities, which were previously reported on the Schedule B (the commercial mortgage schedule). However, absent some form of additional capital relief, any non-conforming CTLs that are reported on Schedule BA would be forced to carry more than 5x the capital vs. if such securities were reported on Schedule B with the requisite commercial mortgage RBC charges. A 30% RBC C1 charge for these securities is not a desirable outcome for PPiA members or for their respective policyholders. Therefore, we would ask that SAPWG make an exception to allow any non-conforming CTLs reported on Schedule BA to carry bond RBC treatment, based on the credit ratings assigned to such securities by a CRP. We understand that such a request is a departure from historical NAIC policy regarding CTLs and would be a temporary exception, limited to only non-conforming CTLs, but we believe such an exception makes sense, given the tight timing for implementing these new rules, and given that this issue will be revisited later, in conjunction with projects to rewrite SSAP No. 43R and to provide a more robust definition of a bond in the SSAPs.

The PPiA understands that some Regulators may be uncomfortable with allowing some non-conforming CTLs to be carried on Schedule D-1 (those for which the SVO assigns a designation), while allowing other non-conforming CTLs to be reported on Schedule BA, yet still carry a bond RBC charge. Such Regulators have stated a preference for an “either/or” approach, rather than providing insurers with “the best of both worlds” (i.e. Schedule D for some securities, and Schedule BA with bond RBC charges for others). If this is truly the case, and Regulators can only see fit to approve one reporting option that grants bond RBC treatment for non-conforming CTLs, then the PPiA requests that all non-conforming CTLs be reported on Schedule BA with the exception granted for bond RBC treatment, based on assigned CRP ratings. The PPiA feels strongly that a 30% RBC charge is a punitive outcome and not appropriate for the risk associated with these securities. As such, we would prefer less punitive capital treatment for the full universe of these securities rather than Schedule D-1 reporting for some (but not all) non-conforming CTLs.

The PPiA shares the NAIC’s desire to provide clarity around this issue and to move forward. We hope to work constructively with the NAIC Staff and with Regulators to develop a final solution that is mutually agreeable and reasonably reflects/reports the risks associated with non-conforming CTLs. However, it is our strong desire to avoid equity RBC treatment for any of these securities—particularly so close to year-end. We would be very appreciative if NAIC Staff and SAPWG would give serious consideration to our proposal, and we stand prepared to answer any questions or offer help, if needed.

Sincerely,

John Petchler

John Petchler, PPiA President, on behalf of the PPiA Board of Directors

CC: Ms. Julie Gann, Assistant Director—Solvency Policy