



Draft date: 10/21/24

FINANCIAL CONDITION (E) COMMITTEE

Thursday, October 24, 2024

11:00 a.m. – 12:00 p.m. ET / 10:00 a.m. – 11:00 a.m. CT / 9:00 – 10:00 a.m. MT / 8:00 – 9:00 a.m. PT

ROLL CALL

Nathan Houdek, Chair	Wisconsin	Mike Chaney	Mississippi
Michael Wise, Vice Chair	South Carolina	Chlora Lindley-Myers	Missouri
Cassie Brown, Vice Chair	Texas	Justin Zimmerman	New Jersey
Michael Conway	Colorado	Adrienne A. Harris	New York
Holly W. Lambert	Indiana	Judith L. French	Ohio
Doug Ommen	Iowa	Elizabeth Kelleher Dwyer	Rhode Island
Vicki Schmidt	Kansas	Scott A. White	Virginia
Kevin P. Beagan	Massachusetts		

NAIC Support Staff: Dan Daveline/Julie Gann/Bruce Jenson

AGENDA

1. Adopt Proposed 2025 Charges — *Nathan Houdek (WI)*
 - American Council of Life Insurers (ACLI) Attachment A
 - Athene Attachment B
2. Draft RFP — *Nathan Houdek (WI)* Attachment D
 - Combined Comment Letters Attachment E
 - (Includes ACLI, Anderson Insights, Bridgeway Analytics
 - NAMIC/APCIA, KBRA, Moody’s Ratings)
3. Any Other Matters Brought Before the Committee — *Nathan Houdek (WI)*

Adopted by the Executive (EX) Committee and Plenary, **Nov. 20, 2024**

Adopted by the Financial Condition (E) Committee, **Oct. 24, 2024**

2024⁵ Charges

FINANCIAL CONDITION (E) COMMITTEE

The mission of the Financial Condition (E) Committee is to be the central forum and coordinator of solvency-related considerations of the NAIC relating to accounting practices and procedures; blanks; valuation of securities; financial analysis and solvency; multistate examinations and examiner and analysis training; and issues concerning insurer insolvencies and insolvency guarantees. In addition, the Committee interacts with the technical task forces.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Financial Condition (E) Committee** will:

A. Monitor all of the changes to the annual/quarterly financial statement blanks and instructions, risk-based capital (RBC) formulas, *Financial Condition Examiners Handbook*, *Accounting Practices and Procedures Manual* (AP&P Manual), *Financial Analysis Handbook*, *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual), NAIC model laws, NAIC accreditation standards, and other NAIC publications.

B. Appoint and oversee the activities of the following: Accounting Practices and Procedures (E) Task Force; Capital Adequacy (E) Task Force; Financial Stability (E) Task Force; Examination Oversight (E) Task Force; Receivership and Insolvency (E) Task Force; Reinsurance (E) Task Force; Risk Retention Group (E) Task Force; and Valuation of Securities (E) Task Force.

C. **Oversee the implementation of the NAIC's "Framework for Regulation of Insurer Investments – A Holistic Review," ensuring that updates or reviews of the Risk-Based Capital (RBC) framework align with the Framework's principles and take into consideration insurers evolving role of the insurance sector in financing the economy and reducing the protection gap.**

~~B-D.~~ Oversee a process to address financial issues that may compromise the consistency and uniformity of the U.S. solvency framework, referring valuation and other issues to the appropriate committees as needed.

~~C-E.~~ Use the Risk-Focused Surveillance (E) Working Group to address specific industry concerns regarding regulatory redundancy, and review any issues that industry subsequently escalates to the Committee.

2. The **Financial Analysis (E) Working Group** will:

A. Analyze nationally significant insurers and groups that exhibit characteristics of trending toward or being financially troubled; determine if appropriate action is being taken.

B. Interact with domiciliary regulators and lead states to assist and advise as to what might be the most appropriate regulatory strategies, methods, and action(s).

C. Support, encourage, promote, and coordinate multistate efforts in addressing solvency problems, including identifying adverse industry trends.

D. Increase information-sharing and coordination between state insurance regulators and federal authorities, including through representation of state insurance regulators in national bodies with responsibilities for system-wide oversight.

3. The **Group Capital Calculation (E) Working Group** will:

A. Continually review and monitor the effectiveness of the group capital calculation (GCC), and consider revisions, as necessary, to maintain the effectiveness of its objective under the U.S. solvency system.

B. Liaise, as necessary, with the International Insurance Relations (G) Committee on international group capital developments, and consider input from participation of U.S. state insurance regulators in the International Association of Insurance Supervisors (IAIS) monitoring process.

FINANCIAL CONDITION (E) COMMITTEE *(Continued)*

4. The **Group Solvency Issues (E) Working Group** will:
 - A. Continue to develop potential enhancements to the current regulatory solvency system as it relates to group solvency-related issues.
 - B. Critically review and provide input and drafting on IAIS material dealing with group supervision issues and identify best practices in group supervision emerging from the IAIS Supervisory Forum.
 - C. Continually review and monitor the effectiveness of the *Insurance Holding Company System Regulatory Act* (#440) and the *Insurance Holding Company System Model Regulation with Reporting Forms and Instructions* (#450), and consider revisions, as necessary, to maintain effective oversight of insurance groups.

5. The **Own Risk and Solvency Assessment (ORSA) Implementation (E) Subgroup** of the Group Solvency Issues (E) Working Group will:
 - A. Continue to provide and enhance an enterprise risk management (ERM) education program for state insurance regulators in support of the ORSA implementation.
 - B. Continually review and monitor the effectiveness of the *Risk Management and Own Risk and Solvency Assessment Model Act* (#505) and its corresponding *NAIC Own Risk and Solvency Assessment (ORSA) Guidance Manual* (ORSA Guidance Manual); consider revisions as necessary.

6. The **Mutual Recognition of Jurisdictions (E) Working Group** will:
 - A. Oversee the process for evaluating jurisdictions, and maintain a listing of jurisdictions that meet the NAIC requirements for recognizing and accepting the NAIC GCC.
 - B. Maintain the *NAIC List of Qualified Jurisdictions* and the *NAIC List of Reciprocal Jurisdictions* in accordance with the *Process for Evaluating Qualified and Reciprocal Jurisdictions*.

7. The **NAIC/American Institute of Certified Public Accountants (AICPA) (E) Working Group** will:
 - A. Continually review the *Annual Financial Reporting Model Regulation* (#205) and its corresponding implementation guide; revise as appropriate.
 - B. Address financial solvency issues by working with the AICPA and responding to AICPA exposure drafts.
 - C. Monitor the federal Sarbanes-Oxley (SOX) Act of 2002, as well as rules and regulations promulgated by the U.S. Securities and Exchange Commission (SEC), the Public Company Accounting Oversight Board (PCAOB), and other financial services regulatory entities.
 - D. Review annually the premium threshold amount included in Section 16 of Model #205, with the general intent that those insurers subject to the Section 16 requirements would capture at least approximately 90% of industry premium and/or in response to any future regulatory or market developments.

FINANCIAL CONDITION (E) COMMITTEE *(Continued)*

8. The **National Treatment and Coordination (E) Working Group** will:
- A. Increase utilization and implementation of the *Company Licensing Best Practices Handbook*.
 - B. Encourage synergies between corporate changes/amendments and rate and form filing review and approval to improve efficiency.
 - C. Continue to monitor the usage and make necessary enhancements to the Form A Database.
 - D. Maintain educational courses in the existing NAIC Insurance Regulator Professional Designation Program for company licensing regulators.
 - E. Make necessary enhancements to promote electronic submission of all company licensing applications.
9. The **Restructuring Mechanisms (E) Working Group** will:
- A. Evaluate and prepare a white paper that:
 - i. Addresses the perceived need for restructuring statutes and the issues those statutes are designed to remedy. Also, consider alternatives that insurers are currently employing to achieve similar results.
 - ii. Summarizes the existing state restructuring statutes.
 - iii. Addresses the legal issues posed by an order of a court (or approval by an insurance department) in one state affecting the policyholders of other states.
 - iv. Considers the impact that a restructuring might have on guaranty associations and policyholders that had guaranty fund protection prior to the restructuring.
 - v. Identifies and addresses the legal issues associated with restructuring using a protected cell.
 - B. Consider requesting approval from the Executive (EX) Committee on developing changes to specific NAIC models as a result of findings from the development of the white paper.
 - C. Develop best practices to be used in considering the approval of proposed restructuring transactions, including, among other things, the expected level of reserves and capital expected after the transfer, along with the adequacy of long-term liquidity needs. Also, develop best practices to be used in monitoring the companies after the transaction is completed. Once completed, recommend to the Financial Regulation Standards and Accreditation (F) Committee for its consideration.
 - D. Consider the need to make changes to the RBC formula to better assess the minimum surplus requirements for companies in runoff.
 - E. Review the various restructuring mechanisms, and develop, if deemed needed, accounting and reporting requirements for referring to the Statutory Accounting Principles (E) Working Group.
10. The **Risk-Focused Surveillance (E) Working Group** will:
- A. Continually review the effectiveness of risk-focused surveillance, and develop enhancements to processes as necessary.
 - B. Continually review regulatory redundancy issues identified by interested parties, and provide recommendations to other NAIC committee groups to address as needed.
 - C. Oversee and monitor the Peer Review Program to encourage consistent and effective risk-focused surveillance processes.
 - D. Continually maintain and update standardized job descriptions/requirements and salary range recommendations for common solvency monitoring positions to assist insurance departments in attracting and maintaining suitable staff.

FINANCIAL CONDITION (E) COMMITTEE *(Continued)*

11. The **Valuation Analysis (E) Working Group** will:

- A. Work with NAIC resources to assist in prioritizing and responding to issues and questions regarding principle-based reserves (PBR) and asset adequacy analysis, including actuarial guidelines or other requirements.
- B. Develop and implement a plan to coordinate PBR reviews/examinations, ~~and provide a confidential forum to address questions and issues.~~
- C. Review, on a targeted basis, asset adequacy analysis filings for *Actuarial Guideline LIII—Application of the Valuation Manual for Testing the Adequacy of Life Insurer Reserves* (AG 53), and coordinate with states as appropriate.
- D. Review, on a targeted basis, long-term care (LTC) reserve adequacy filings for *Actuarial Guideline LI—The Application of Asset Adequacy Testing to Long-Term Care Insurance Reserves* (AG 51), and coordinate with states as appropriate.
- E. Provide a confidential forum to address questions/issues regarding ~~reinsurance risk transfer with respect to PBR~~ ~~and~~ asset adequacy analysis, as well as related reinsurance risk transfer issues, and make referrals, as appropriate, to other NAIC regulator groups.
- F. Refer questions/issues, as appropriate, to the Life Actuarial (A) Task Force that may require consideration of changes/interpretations to be provided in the *Valuation Manual* or related actuarial guidelines.
- G. Assist NAIC resources in the use of models and other analytical tools to support the review of PBR/asset adequacy analysis.
- H. Make referrals, as appropriate, to the Financial Analysis (E) Working Group.
- I. Perform other work to carry out the Valuation Analysis (E) Working Group procedures.

NAIC Support Staff: Dan Daveline/Julie Gann/Bruce Jenson

Adopted by the Executive (EX) Committee and Plenary, Nov. 20, 2024

Adopted by the Financial Condition (E) Committee, Oct. 24, 2024

Adopted by the Accounting Practices and Procedures (E) Task Force, Aug. 14, 2024

2024⁵ Charges

ACCOUNTING PRACTICES AND PROCEDURES (E) TASK FORCE

The mission of the Accounting Practices and Procedures (E) Task Force is to identify, investigate, and develop solutions to accounting problems with the ultimate goal of guiding insurers in properly accounting for various aspects of their operations; modify the *Accounting Practices and Procedures Manual* (AP&P Manual) to reflect changes necessitated by Task Force action; and study innovative insurer accounting practices that affect the ability of state insurance regulators to determine the true financial condition of insurers.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Accounting Practices and Procedures (E) Task Force** will:
 - A. Oversee the activities of the Blanks (E) Working Group and the Statutory Accounting Principles (E) Working Group.
2. The **Blanks (E) Working Group** will:
 - A. Consider improvements and revisions to the various annual/quarterly statement blanks to:
 - i. Conform these blanks to changes made in other areas of the NAIC to promote uniformity in reporting of financial information by insurers.
 - ii. Develop reporting formats for other entities subject to the jurisdiction of state insurance departments.
 - iii. Conform the various NAIC blanks and instructions to adopted NAIC policy.
 - iv. Oversee the development of additional reporting formats within the existing annual financial statements as needs are identified.
 - B. Continue to monitor state filing checklists to maintain current filing requirements.
 - C. Continue to monitor and improve the quality of financial data filed by insurance companies by recommending improved or additional language for the *Annual Statement Instructions*.
 - D. Continue to monitor and review all proposals necessary for the implementation of statutory accounting guidance to ensure proper implementation of any action taken by the Accounting Practices and Procedures (E) Task Force affecting annual financial statements and/or instructions.
 - E. Continue to coordinate with other task forces of the NAIC to ensure proper implementation of reporting and instructions changes as proposed by these taskforces.
 - F. Coordinate with the applicable task forces and working groups as needed to avoid duplication of reporting within the annual and quarterly statement blanks.
 - G. Consider proposals presented that would address duplication in reporting, eliminate data elements, financial schedules and disclosures that are no longer needed, and coordinate with other NAIC task forces and working groups if applicable, to ensure revised reporting still meets the needs of regulators.
 - H. Review requests for investment schedule blanks and instructions changes in connection with the work being performed by the Capital Adequacy (E) Task Force and its working groups.
 - I. Review changes requested by the Valuation of Securities (E) Task Force relating to its work on other invested assets reporting for technical consistency within the investment reporting schedules and instructions.

ACCOUNTING PRACTICES AND PROCEDURES (E) TASK FORCE *(Continued)*

3. The **Statutory Accounting Principles (E) Working Group** will:
- A. Maintain codified statutory accounting principles by providing periodic updates to the guidance that address new statutory issues and new U.S. generally accepted accounting principles (GAAP) pronouncements. Provide authoritative responses to questions of application and clarifications for existing statutory accounting principles. Report all actions and provide updates to the Accounting Practices and Procedures (E) Task Force.
 - B. At the discretion of the Working Group chair, develop comments on exposed U.S. GAAP and International Financial Reporting Standards (IFRS) pronouncements affecting financial accounting and reporting. Any comments are subject to review and approval by the chairs of the Accounting Practices and Procedures (E) Task Force and the Financial Condition (E) Committee.
 - C. Coordinate with the Life Actuarial (A) Task Force on changes to the AP&P Manual related to the *Valuation Manual* VM-A, Requirements, and VM-C, Actuarial Guidelines, as well as other *Valuation Manual* requirements. This process will include the receipt of periodic reports on changes to the *Valuation Manual* on items that require coordination.
 - D. Obtain, analyze, and review information on permitted practices, prescribed practices, or other accounting treatments suggesting that issues or trends occurring within the industry may compromise the consistency and uniformity of statutory accounting, including, but not limited to, activities conducted by insurers for which there is currently no statutory accounting guidance or where the states have prescribed statutory accounting that differs from the guidance issued by the NAIC. Use this information to consider possible changes to statutory accounting.

NAIC Support Staff: Robin Marcotte

Adopted by the Executive (EX) Committee and Plenary, **Nov. 20, 2024**

Adopted by the Financial Condition (E) Committee, **Oct. 24, 2024**

Adopted by the Capital Adequacy (E) Task Force, Sept. 26, 2024

2024⁵ Charges

CAPITAL ADEQUACY (E) TASK FORCE

The mission of the Capital Adequacy (E) Task Force is to evaluate and recommend appropriate refinements to capital requirements for all types of insurers.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Capital Adequacy (E) Task Force** will:
 - A. Evaluate emerging “risk” issues for referral to the risk-based capital (RBC) working groups/subgroups for certain issues involving more than one RBC formula. Monitor emerging and existing risks relative to their consistent or divergent treatment in the three RBC formulas.
 - B. Review and evaluate company submissions for the schedule and corresponding adjustment to total adjusted capital (TAC).
 - C. Evaluate relevant historical data, and apply defined statistical safety levels over appropriate time horizons in developing recommendations for revisions to the current asset risk structure and factors in each of the RBC formulas.

2. The **Health Risk-Based Capital (E) Working Group, Life Risk-Based Capital (E) Working Group, and Property and Casualty Risk-Based Capital (E) Working Group** will:
 - A. Evaluate refinements to the existing NAIC RBC formulas implemented in the prior year. Forward the final version of the structure of the current year life and fraternal, property/casualty (P/C), and health RBC formulas to the Financial Condition (E) Committee by June.
 - B. Consider improvements and revisions to the various RBC blanks to: 1) conform the RBC blanks to changes made in other areas of the NAIC to promote uniformity; and 2) oversee the development of additional reporting formats within the existing RBC blanks as needs are identified. Any proposal that affects the RBC structure must be adopted no later than ~~April 30~~**May 15** of the reporting year, and any proposal that affects the RBC factors and/or instructions must be adopted no later than June 30 of the reporting year. Adopted changes will be forwarded to the Financial Condition (E) Committee by the next scheduled meeting. Any adoptions made to the annual financial statement blanks or statutory accounting principles that affect an RBC change adopted by June 30 and result in an amended change may be considered by and adopted by July 30, where the Capital Adequacy (E) Task Force votes to pursue by **super-majority (two-thirds)** consent of members.
 - C. Monitor changes in accounting and reporting requirements resulting from the adoption and continuing maintenance of the revised *Accounting Practices and Procedures Manual* (AP&P Manual) to ensure that model laws, publications, formulas, analysis tools, etc., supported by the Task Force continue to meet regulatory objectives.
 - D. Review the effectiveness of the NAIC’s RBC policies and procedures as they affect the accuracy, audit ability, timeliness of reporting access to RBC results, and comparability between the RBC formulas. Report on data quality problems in the prior year RBC filings at the summer and fall national meetings.

CAPITAL ADEQUACY (E) TASK FORCE *(continued)*

3. The **Longevity Risk (E/A) Subgroup** of the Life Risk-Based Capital (E) Working Group and the Life Actuarial (A) Task Force will:
 - A. Provide recommendations for the appropriate treatment of longevity risk transfers by the new longevity factors.

4. The **Variable Annuities Capital and Reserve (E/A) Subgroup** of the Life Risk-Based Capital (E) Working Group and the Life Actuarial (A) Task Force will:
 - A. Monitor the impact of the changes to the variable annuities reserve framework and RBC calculation, and determine if additional revisions need to be made.
 - B. Develop and recommend appropriate changes, including those to improve accuracy and clarity of variable annuity (VA) capital and reserve requirements.

5. The **Catastrophe Risk (E) Subgroup** of the Property and Casualty Risk-Based Capital (E) Working Group will:
 - A. Recalculate the premium risk factors on an ex-catastrophe basis, if needed.
 - B. Continue to update the U.S. and non-U.S. catastrophe event list.
 - C. Continue to evaluate the need for exemption criteria for insurers with minimal risk.
 - D. Evaluate the RBC results inclusive of a catastrophe risk charge.
 - E. Refine instructions for the catastrophe risk charge.
 - F. Continue to evaluate any necessary refinements to the catastrophe risk formula.
 - G. Evaluate other catastrophe risks for possible inclusion in the charge.

6. The **Risk-Based Capital Investment Risk and Evaluation (E) Working Group** will:
 - A. Perform a comprehensive review of the RBC investment framework for all business types, which could include:
 1. Identifying and acknowledging uses that extend beyond the purpose of the *Risk-Based Capital (RBC) for Insurers Model Act* (#312).
 2. Assessing the impact and effectiveness of potential changes in contributing to the identification of weakly capitalized companies; i.e., those companies at action levels.
 3. Documenting the modifications made over time to the formulas, including, but not limited to, an analysis of the costs in study and development, implementation (internal and external), assimilation, verification, analysis, and review of the desired change to the RBC formulas and facilitating the appropriate allocation of resources.

7. The **Generator of Economic Scenarios (GOES) (E/A) Subgroup** of the Life Risk-Based Capital (E) Working Group and the Life Actuarial (A) Task Force will:
 - A. Monitor that the economic scenario governance framework is being appropriately followed by all relevant stakeholders involved in scenario delivery.
 - B. Review material economic scenario generator updates, either driven by periodic model maintenance or changes to the economic environment and provide recommendations.
 - C. Regularly review key economic conditions and metrics to evaluate the need for off-cycle or significant economic scenario generator updates and maintain a public timeline for economic scenario generator updates.
 - D. Support the implementation of an economic scenario generator for use in statutory reserve and capital calculations.
 - E. Develop and maintain acceptance criteria that reflect history as well as plausibly more extreme scenarios.

NAIC Support Staff: Eva Yeung

Adopted by the Executive (EX) Committee and Plenary, Nov. 20, 2024

Adopted by the Financial Condition (E) Committee, Oct. 24, 2024

Adopted by the Examination Oversight (E) Task Force, Sept. 25, 2024

2024⁵ Charges

EXAMINATION OVERSIGHT (E) TASK FORCE

The mission of the Examination Oversight (E) Task Force is to monitor, develop, and implement tools for the risk-focused surveillance process. For financial examinations and analysis, this includes maintenance of the *Financial Condition Examiners Handbook* and the *Financial Analysis Handbook* to provide guidance to examiners and analysts using a risk-focused approach to solvency regulation and to encourage effective communication and coordination between examiners, analysts, and other regulators. In addition, the mission of the Task Force is to: monitor and refine regulatory tools of the risk-focused surveillance process, including Financial Analysis Solvency Tools (FAST) such as company profiles and the FAST ratio scoring system; oversee financial examiner and analyst use of electronic software tools; monitor the progress of coordination efforts among the states in conducting examinations and the sharing of information necessary to solvency monitoring; establish procedures for the flow of information between the states about troubled companies; maintain an effective approach to the review of information technology (IT) general controls; and monitor the timeliness of financial examinations.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Examination Oversight (E) Task Force** will:
 - A. Accomplish its mission using the following groups:
 - i. Electronic Workpaper (E) Working Group.
 - ii. Financial Analysis Solvency Tools (E) Working Group.
 - iii. Financial Examiners Coordination (E) Working Group.
 - iv. Financial Examiners Handbook (E) Technical Group.
 - v. Information Technology (IT) Examination (E) Working Group.
2. The **Electronic Workpaper (E) Working Group** will:
 - A. Monitor and support the state insurance departments in using electronic workpaper software tools to conduct and document solvency monitoring activities.
 - B. Provide ongoing oversight to the transition of electronic workpaper work to the TeamMate+ application.
 - C. Monitor state insurance regulator use of TeamMate+ to proactively identify best practices and improvements to the application, as necessary.
3. The **Financial Analysis Solvency Tools (E) Working Group** will:
 - A. Provide ongoing maintenance and enhancements to the *Financial Analysis Handbook* and related applications for changes to the NAIC annual/quarterly financial statement blanks, for input from other regulators, and for the work of, or referrals from, other NAIC committees, task forces, and working groups to develop enhancements to risk-focused analysis and monitoring of the financial condition of insurance companies and groups.
 - B. Provide ongoing development maintenance and enhancements to the automated financial solvency tools developed to assist in conducting risk-focused analysis and monitoring the financial condition of insurance companies and groups. Prioritize and perform analysis to ensure that the tools remain reliable and accurate.

EXAMINATION OVERSIGHT (E) TASK FORCE (Continued)

- C. Coordinate with the Financial Examiners Handbook (E) Technical Group and the Risk-Focused Surveillance (E) Working Group, as appropriate, to develop and maintain guidance in order to provide effective solvency monitoring.
4. The **Financial Examiners Coordination (E) Working Group** will:
- A. Develop enhancements that encourage the coordination of examination activities regarding holding company groups.
 - B. Promote coordination by assisting and advising domiciliary regulators and exam coordinating states as to what might be the most appropriate regulatory strategies, methods, and actions regarding financial examinations of holding company groups.
 - C. Facilitate communication among regulators regarding common practices and issues arising from coordinating examination efforts.
 - D. Provide ongoing maintenance and enhancements to the Financial Examination Electronic Tracking System (FEETS).
5. The **Financial Examiners Handbook (E) Technical Group** will:
- A. Continually review the *Financial Condition Examiners Handbook* and revise, as appropriate.
 - B. Coordinate with the Risk-Focused Surveillance (E) Working Group to monitor the implementation of the risk- assessment process by developing additional guidance and exhibits within the *Financial Condition Examiners Handbook*, including consideration of potential redundancies affected by the examination process, corporate governance, and other guidance as needed to assist examiners in completing financial condition examinations.
 - C. Coordinate with the Financial Analysis Solvency Tools (E) Working Group and the Risk-Focused Surveillance (E) Working Group, as appropriate, to develop and maintain guidance in order to provide effective solvency monitoring.
 - D. Coordinate with the IT Examination (E) Working Group and the Financial Examiners Coordination (E) Working Group to maintain specialized areas of guidance within the *Financial Condition Examiners Handbook* related to the charges of these specific working groups.
6. The **Information Technology (IT) Examination (E) Working Group** will:
- A. Continually review, develop, and revise guidance in the *Financial Condition Examiners Handbook* and other related tools, as needed, to address information technology risks.
 - B. Coordinate with the Cybersecurity (H) Working Group to monitor cybersecurity trends, including emerging and/or ongoing vulnerabilities, and develop guidance within the *Financial Condition Examiners Handbook* or other tools, if deemed necessary, to support IT examiners.

NAIC Support Staff: Bailey Henning

Adopted by the Executive (EX) Committee and Plenary, Nov. 20, 2024

Adopted by the Financial Condition (E) Committee, Oct. 24, 2024

Adopted by the Financial Stability (E) Task Force, Oct. 17, 2024

2024⁵ Charges

FINANCIAL STABILITY (E) TASK FORCE

The mission of the Financial Stability (E) Task Force is to consider issues concerning domestic or global financial stability as they pertain to the role of state insurance regulators.

Ongoing Support of NAIC Program, Products, or Services

1. The **Financial Stability (E) Task Force** will:
 - A. Manage the macroprudential supervisory component of the NAIC financial solvency framework.
 - i. Monitor the U.S. insurance industry's macroprudential risk levels.
 - ii. Maintain macroprudential regulatory tools.
 - iii. Identify data gaps and enhanced disclosure needs for the statutory financial statement and/or other reporting mechanisms.
 - iv. Propose enhancements and/or additional supervisory measures to the Financial Condition (E) Committee or other relevant committees, and consult with such committees on implementation.
 - B. Monitor U.S. macroprudential policy issues, and respond as appropriate.
 - i. Support and work with the state insurance regulator representative to the Financial Stability Oversight Council (FSOC) to address confidential FSOC or other federal agency macroprudential work.
 - ii. Participate in public FSOC or other federal agency macroprudential work.
 - C. Monitor international macroprudential policy issues, and participate/respond as appropriate.
 - i. Coordinate with the International Insurance Relations (G) Committee to address International Association of Insurance Supervisors (IAIS) or other international macroprudential work.

2. The **Macroprudential (E) Working Group** will:
 - A. Oversee the implementation and maintenance of the Liquidity Stress Testing Framework (LST Framework).
 - B. Monitor domestic and global activities including those enumerated in the "Plan for the List of Macroprudential Working Group (MWG) Considerations document.
 - C. Execute the original Macroprudential Initiative (MPI) projects related to counterparty disclosures and capital stress testing.
 - D. Continue to develop and administer data collection tools as needed, leveraging existing data where feasible, to provide the Financial Stability (E) Task Force with meaningful macroprudential information regarding how the insurance sector is navigating the prevailing market conditions.
 - E. Oversee the development, implementation, and maintenance process for a new Macroprudential Risk Assessment system (i.e., policies, procedures, and tools) to enhance regulators' ability to monitor industry trends from a macroprudential perspective.
 - F. Oversee the documentation of the NAIC's macroprudential policies, procedures, and tools.
 - G. Provide the Task Force with updates to IAIS and other international initiatives as needed.

NAIC Support Staff: Tim Nauheimer/Todd Sells

Adopted by the Executive (EX) Committee and Plenary, **Nov. 20, 2024**

Adopted by the Financial Condition (E) Committee, **Oct. 24, 2024**

Adopted by the Receivership and Insolvency (E) Task Force, Aug. 14, 2024

2024~~5~~ Charges

RECEIVERSHIP AND INSOLVENCY (E) TASK FORCE

The mission of the Receivership and Insolvency (E) Task Force is to be administrative and substantive as it relates to issues concerning insurer insolvencies and insolvency guarantees. Such duties include, without limitation: 1) monitoring the effectiveness and performance of the state administration of receiverships and the state guaranty fund system; 2) coordinating cooperation and communication among state insurance regulators, receivers, and guaranty funds; 3) monitoring ongoing receiverships and reporting on such receiverships to NAIC members; 4) developing and providing educational and training programs in the area of insurer insolvencies and insolvency guarantees to state insurance regulators, professionals, and consumers; 5) developing and monitoring relevant model laws, guidelines, and products; and 6) providing resources for state insurance regulators and professionals to promote efficient operations of receiverships and guaranty funds.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Receivership and Insolvency (E) Task Force** will:
 - A. Monitor and promote efficient operations of insurance receiverships and guaranty associations.
 - B. Monitor and promote state adoption of insurance receivership and guaranty association model acts and regulations, and monitor other legislation related to insurance receiverships and guaranty associations.
 - C. Provide input and comments to the International Association of Insurance Supervisors (IAIS), the Financial Stability Board (FSB), ~~and/or~~ other related groups on issues regarding international resolution authority.
 - D. Monitor, review, and provide input on federal rulemaking and studies related to insurance receiverships.
 - E. Provide an ongoing review of the *Receiver's Handbook for Insurance Company Insolvencies* (Receiver's Handbook), other related NAIC publications, and the Global Receivership Information Database (GRID), and make any necessary updates.
 - F. Monitor the work of other NAIC committees, task forces, and working groups to identify and address any issues that affect receivership law and/or regulatory guidance.
 - G. Perform additional work as directed by the Financial Condition (E) Committee and/or received through referrals by other groups.

2. The **Receivership Financial Analysis (E) Working Group** will:
 - A. Monitor receiverships involving nationally significant insurers/groups to support, encourage, promote, and coordinate multistate efforts in addressing problems.
 - B. Interact with the Financial Analysis (E) Working Group, domiciliary regulators, and lead states to assist and advise ~~as to what might be on~~ the most appropriate regulatory strategies, methods, and/or action(s) regarding potential or pending receiverships.

3. The **Receivership Law (E) Working Group** will:
 - A. Review and provide recommendations on any issues identified that may affect states' receivership and guaranty association laws (e.g., any issues that arise as a result of market conditions; insurer insolvencies; federal rulemaking and studies; international resolution initiatives; or the work performed by or referred from other NAIC committees, task forces, and/or working groups).
 - B. Discuss significant cases that may affect the administration of receiverships.

RECEIVERSHIP AND INSOLVENCY (E) TASK FORCE *(Continued)*

NAIC Support Staff: Jane Koenigsman

Adopted by the Executive (EX) Committee and Plenary, **Nov. 20, 2024**

Adopted by the Financial Condition (E) Committee, **Oct. 24, 2024**

Adopted by the Reinsurance (E) Task Force, July 22, 2024

2024⁵ Charges

REINSURANCE (E) TASK FORCE

The mission of the Reinsurance (E) Task Force is to monitor and coordinate activities and areas of interest that overlap to some extent the charges of other NAIC groups—specifically, the International Insurance Relations (G) Committee.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Reinsurance (E) Task Force** will:
 - A. Provide a forum for the consideration of reinsurance-related issues of public policy.
 - B. Oversee the activities of the Reinsurance Financial Analysis (E) Working Group.
 - C. Coordinate with the Mutual Recognition of Jurisdictions (E) Working Group on matters regarding reinsurance.
 - ~~C~~.D. Communicate and coordinate with the Federal Insurance Office (FIO), other federal authorities, and international regulators and authorities on matters pertaining to reinsurance.
 - E. Monitor reinsurance-related activities of other task forces and working groups at the NAIC.
 - ~~D~~.F. Consider any other issues related to ~~the revised~~ Model #785, Model #786, and Model #787.
 - ~~E~~.G. Monitor the development of international principles, standards, and guidance with respect to reinsurance. This includes, but is not limited to, monitoring the activities of various groups within the International Association of Insurance Supervisors (IAIS), including the Reinsurance and Other Forms of Risk Transfer Subcommittee, the Reinsurance Mutual Recognition Subgroup, and the Reinsurance Transparency Group.
 - ~~F~~.H. Consider the impact of reinsurance-related federal legislation, including, but not limited to, the federal Nonadmitted and Reinsurance Reform Act (NRRRA) and the Federal Insurance Office Act, and coordinate any appropriate NAIC action.
 - ~~G~~.I. Continue to monitor the impact of reinsurance-related international agreements, including the “Bilateral Agreement Between the United States of America and the European Union on Prudential Measures Regarding Insurance and Reinsurance” (EU Covered Agreement) and the “Bilateral Agreement Between the United States of America and the United Kingdom on Prudential Measures Regarding Insurance and Reinsurance” (UK Covered Agreement).
2. The **Reinsurance Financial Analysis (E) Working Group** will:
 - A. Operate in regulator-to-regulator session, pursuant to paragraph 3 (specific companies, entities or individuals) of the NAIC Policy Statement on Open Meetings, and operate in open session when discussing certified reinsurance topics and policy issues, such as amendments to the Uniform Application for ~~C~~ertified or ~~R~~eciprocal Jurisdiction Reinsurers.
 - B. Provide advisory support and assistance to states in the review of reinsurance collateral reduction applications. Such a process with respect to the review of applications for reinsurance collateral reduction and qualified jurisdictions should strengthen state regulation and prevent regulatory arbitrage.
 - C. Provide a forum for discussion among NAIC jurisdictions of reinsurance issues related to specific companies, entities, or individuals.
 - D. Support, encourage, promote, and coordinate multistate efforts in addressing issues related to certified reinsurers, including, but not limited to, multistate recognition of certified or reciprocal jurisdiction reinsurers.

REINSURANCE (E) TASK FORCE *(Continued)*

- E. Provide analytical expertise and support to the states with respect to certified reinsurers, reciprocal jurisdiction reinsurers, and applicants.
- F. Provide advisory support with respect to issues related to the determination of qualified jurisdictions.
- G. Ensure the public passporting website remains current.

NAIC Support Staff: Jake Stultz/Dan Schelp

Adopted by the Executive (EX) Committee and Plenary, Nov. 20, 2024

Adopted by the Financial Condition (E) Committee, Oct. 24, 2024

Adopted by the Risk Retention Group (E) Task Force, July 24, 2024

2024⁵ Charges

RISK RETENTION GROUP (E) TASK FORCE

The mission of the Risk Retention Group (E) Task Force is to stay apprised of the work of other NAIC groups as it relates to financial solvency regulation and the NAIC Financial Regulation Standards and Accreditation Program. The Task Force may make referrals to the Financial Regulation Standards and Accreditation (F) Committee and/or other NAIC groups, as deemed appropriate.

Ongoing Support of NAIC Programs, Products, or Services

1. The **Risk Retention Group (E) Task Force** will:
 - A. Monitor and evaluate the work of other NAIC committees, task forces, and working groups that may affect the filing requirements or compliance of related to risk retention groups (RRGs) (e.g., Specifically, if any of these actions that affect compliance with the the NAIC Financial Regulation and Accreditation Standards Program, assess whether and/or how the changes should apply to RRGs and their affiliates.
 - B. Monitor and analyze review any federal activitiesactions, including any U.S. Government Accountability Office (GAO) reports, and .-Cconsider any action necessary action as a result of federal activity.
 - C. Monitor the impacts of recent tools and resources made available to domiciliary and non-domiciliary state insurance regulators pertaining to of RRGs. Consider whether additional action is necessary, including educational programs or enhancements or the development of new opportunities, updating resources, and further clarifications.

NAIC Support Staff: Becky Meyer/Sara Franson

Adopted by the Executive (EX) Committee and Plenary, **Nov. 20, 2024**

Adopted by the Financial Condition (E) Committee, **Oct. 24, 2024**

Adopted by the Valuation of Securities (E) Task Force, Aug. 13, 2024

2024⁵ Proposed Charges

VALUATION OF SECURITIES (E) TASK FORCE

The mission of the Valuation of Securities (E) Task Force is to provide regulatory leadership and expertise to establish and maintain all aspects of the NAIC's credit assessment process for insurer-owned securities, as well as produce insightful and actionable research and analysis regarding insurer investments.

Ongoing Support of NAIC Programs, Products or Services

1. The **Valuation of Securities (E) Task Force** will:
 - A. Review and monitor the operations of the NAIC Securities Valuation Office (SVO) and the NAIC Structured Securities Group (SSG) to ensure they continue to reflect regulatory objectives.
 - B. Maintain and revise the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) to provide solutions to investment-related regulatory issues for existing or anticipated investments.
 - C. Monitor changes in accounting and reporting requirements resulting from the continuing maintenance of the *Accounting Practices and Procedures Manual*, as well as financial statement blanks and instructions, to ensure that the P&P Manual continues to reflect regulatory needs and objectives.
 - D. Consider whether improvements should be suggested to the measurement, reporting and evaluation of invested assets by the NAIC as the result of: 1) newly identified types of invested assets; 2) newly identified investment risks within existing invested asset types; or 3) elevated concerns regarding previously identified investment risks.
 - E. Identify potential improvements to the credit filing process, including formats and electronic system enhancements.
 - F. Provide effective direction to the NAIC's mortgage-backed securities modeling firms and consultants.
 - G. Coordinate with other NAIC working groups and task forces—including, but not limited to, the Capital Adequacy (E) Task Force, the Statutory Accounting Principles (E) Working Group, the Blanks (E) Working Group, ~~and the~~ Risk-Based Capital Investment Risk & Evaluation (E) Working Group, and the Valuation Analysis (E) Working Group—to formulate recommendations and to make referrals to such other NAIC regulator groups to ensure expertise relative to investments, or the purpose and objective of guidance in the P&P Manual, is reflective in the guidance of such other groups and that the expertise of such other NAIC regulatory groups and the objectives of their guidance is reflected in the P&P Manual.
 - H. Identify potential improvements to the filing exempt process (the use of credit rating provider ratings to determine an NAIC designation) to ensure greater consistency, uniformity and appropriateness to achieve the NAIC's financial solvency objectives.
 - I. Implement policies to oversee the NAIC's staff administration of rating agency ratings used in NAIC processes, including staff's discretion over the applicability of their use in its administration of filing exemption.
 - J. Establish criteria to permit staff's discretion over the assignment of NAIC designations for securities subject to the filing exempt process (the use of credit rating provider ratings to determine an NAIC designation) to ensure greater consistency, uniformity and appropriateness to achieve the NAIC's financial solvency objectives.
 - K. Implement additional and alternative ways to measure and report investment risk.

NAIC Support Staff: Charles Therriault



October 14, 2024

Commissioner Nathan Houdek, Chair
Financial Condition (E) Committee
National Association of Insurance Commissioners
Via email ddaveline@naic.org

Re: Comments on E Committee proposed 2025 charges

Submitted Electronically

Dear Commissioner Houdek,

The American Council of Life Insurers (ACLI) appreciates the opportunity to comment on the E Committee's August 2, 2024, request for comments on the proposed 2025 charges for the Financial Condition ("E") Committee.

ACLI's comments pertain to the updated charges for the Reinsurance Task Force. ACLI supports the addition of charge 1.E, which directs the Reinsurance Task Force to *"monitor reinsurance-related activities of other task forces and working groups at the NAIC."*

At a time when the NAIC is working concurrently on multiple projects related to reinsurance, investing the Reinsurance Task Force with the directive to monitor reinsurance-related activities – regardless of letter-committee jurisdiction – is a positive development. We were also pleased to see that the Life Actuarial ("A") Task Force proposed 2025 charges included a direction to *"coordinate with the Reinsurance (E) Task Force on actuarial items related to reinsurance."* These charges reflect the NAIC's stated commitment to promoting coordination between regulators who are working on related issues in different groups.

This type of cooperation and information-sharing between different working groups is essential to ensure that regulators and stakeholders understand the cumulative impacts of related workstreams. The stakes are high – reinsurance is a critical component of the insurance ecosystem whose value goes beyond simply compensating insurance companies in the event of loss. Life reinsurance is a critical risk management tool used by insurers to spread risk and manage capital. The capital efficiency provided by life reinsurers is particularly helpful to life insurers issuing new policies because initial costs (expenses plus reserves) are often higher than the premiums received. Sharing those initial costs with a reinsurer alleviates strain on capital, which ultimately helps life insurers to fulfill their role of providing protection and retirement savings to society.

Insurers leverage life reinsurance to improve underwriting results, increase underwriting capacity, support entry and exit from insurance markets, promote diversification. Reinsurance risk transfer

American Council of Life Insurers | 101 Constitution Ave, NW, Suite 700 | Washington, DC 20001-2133

The American Council of Life Insurers 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 93 percent of industry assets in the United States.

acll.com

fosters financial stability by smoothing the impact of unexpected losses on financial statements. Reinsurers' experience in analyzing, identifying and modeling risks often make reinsurers key drivers in the adoption of better risk management practices by many organizations. And because reinsurers invest the premiums they generate on a long-term basis in a range of different financial assets, reinsurers contribute capital to the real economy, which supports the production and delivery of goods and services.

ACLI looks forward to continuing to work collaboratively with regulators to address reinsurance-related issues. We appreciate the willingness of E committee working groups, like the Statutory Accounting Principles Working Group, to engage in thoughtful, ongoing dialogue with the industry and regulators on a variety of issues, including reinsurance-related issues. This type of ongoing dialogue can help deepen industry's understanding of regulatory objectives, which helps facilitate more productive information-exchanges and ultimately promotes more constructive responses to proposed regulatory solutions. Additionally, these discussions provide an opportunity for regulators to further their understanding of the changes occurring in the industry.

Thank you for the opportunity to share these views. Please don't hesitate to reach out if you have any questions, concerns, or if there is anything ACLI can do to provide assistance.

Sincerely,

A handwritten signature in black ink that reads "Mariana Gomez-Vock". The signature is written in a cursive, flowing style.

Mariana Gomez-Vock



October 14, 2024

Dan Daveline, Director, Financial Regulatory Services
 National Association of Insurance Commissioners
 1100 Walnut Street, Suite 1500
 Kansas City, MO 64106-2197
 Via email: ddaveline@naic.org

RE: Combined Comments on the Revised Framework for Regulation of Insurer Investments and Proposed 2025 E-Committee Charges

Dear Mr. Daveline:

From the initial exposure of the proposed *Framework for Regulation of Insurer Investments – A Holistic Review* (the “Framework”), Athene Holding, Ltd. (“Athene”) has been a strong supporter of the Financial Condition (E) Committee’s direction. The Framework represents a thoughtful and comprehensive approach to addressing one of the most pressing challenges faced by U.S. insurance regulators. With the life insurance sector evolving rapidly and the ongoing retirement savings crisis demanding greater attention, the Framework offers a generational opportunity to modernize the RBC system and advance a state-based solution.

The workstreams initiated under the Framework are complex and interconnected, and given that asset risk (C-0 and C-1) now represents the largest component of life insurer capital (72%¹), their outcomes will directly influence how the life insurance industry continues to provide long-term retirement solutions to millions of consumers. We offer the following combined comments on both the Framework and the proposed 2025 E-Committee Charges in a continuing effort to support the NAIC’s important work.

Global Context and Importance of NAIC’s Work

We believe that the NAIC’s work on the Framework is crucial not just domestically but globally. Life insurer investments have come under increasing scrutiny from policymakers and regulators around the world as financial markets undergo transformative shifts. In the U.S., the RBC regime supports critical insurer investment in the real economy and beneficial diversification away from bank financing. As of 2023, insurers held ~13% of U.S. non-government debt, compared with only ~6% in the case of the E.U. The growing importance of insurers’ roles in the real economy, particularly in funding infrastructure, renewable energy, and other long-term projects, highlights the critical balancing act regulators must perform between supporting healthy capital markets and ensuring prudential stability.

State insurance regulators, through the NAIC, are playing an increasingly pivotal role in navigating this evolving landscape. Their leadership in managing risk while promoting investment in the real economy has drawn the attention of regulatory bodies in Europe and Asia and international standard setters. The Framework represents one of the first comprehensive regulatory responses to the shifting financial environment, positioning the NAIC as a global leader. However, to maintain

¹ See https://content.naic.org/sites/default/files/national_meeting/lrbcbwg-materials-20240814.pdf, p. 13.

this momentum, it is essential that the vision for leadership presented by the Framework is realized to further showcase the viability of a state-based regulatory solution that is congruous, adaptable, and forward-looking.

Moreover, as the U.S. continues to promote a workable alternative to the IAIS's insurance capital standard, it is critical that the U.S. can hold out the RBC regime as a modern and effective regulatory tool. RBC is a key input into the Aggregation Method and is subject to careful examination internationally for ICS equivalency.

Engagement with International Policymakers

Over the last year, senior executives from Apollo and Athene have engaged with international regulatory bodies, including the NAIC, to provide insights on the current market transformation and the role of private credit in our modern financial ecosystem. As part of those discussions, we have highlighted the NAIC's holistic approach as a potential blueprint for other jurisdictions. In our discussions with foreign policymakers and regulators, we have praised the Framework for its balanced vision, and we have underscored that the NAIC's leadership is setting a global standard for others to follow. The path laid out by the NAIC could serve as a model for integrating prudential supervision with the need to prudently stimulate economic growth through life insurers' long-term investments. However, in order for the Framework's vision to be fully realized, it must be clearly and effectively implemented and applied not only to current workstreams but also serve as the foundational basis for the E-Committee's work in the coming years.

Ongoing Challenges and Opportunities with Existing E-Committee Activities

While we are encouraged by the work already underway, we must also recognize that some ongoing initiatives remain, in our view, inconsistent with the Framework's guiding principles. The workstreams cited within the Framework are essential to progress, but several key areas remain fragmented or misaligned with its holistic objectives. For example, the identification of comparable attributes for CLOs by the Academy will impact the Securities Valuation Office's modeling of these instruments. The Framework underscores the need for consistency across asset classes, yet this particular workstream may introduce variations that are not fully aligned with the Framework's coordinated approach to risk evaluation and perpetuate long-standing inconsistencies already present within RBC.

We believe it important that the E-Committee (or some other leadership group within the NAIC) regularly evaluate all ongoing work through the lens of the Framework to ensure alignment with its principles. We encourage the Financial Condition Committee to stay directly engaged in refining these workstreams, ensuring that the regulatory system for insurers continues to evolve in a manner that strengthens solvency protections while allowing the industry to effectively contribute to the broader economy and mitigate the retirement gap.

Proposed Additions to the 2025 E-Committee Charges

As the NAIC continues its commendable efforts to modernize regulatory frameworks for insurer investments, we believe it is essential that the 2025 charges explicitly reflect the NAIC's continued commitment to the Framework and the important role of commissioner oversight and direction, reinforcing the RBC system's foundational role in maintaining solvency and enabling the insurance

industry to support long-term economic growth. By incorporating these priorities, the NAIC can continue to lead on a global scale while ensuring that our regulatory systems remain robust, responsive, and forward-looking. The current charges include no such references.

As discussed, the Framework provides a comprehensive and forward-looking approach to addressing the evolving challenges facing the insurance industry, especially considering changing market dynamics and increasing regulatory scrutiny. The Framework also serves as an opportunity to provide a consistent and holistic lens to the various investment-related initiatives at the NAIC.

Successful implementation of the Framework's principles and goals hinges on this Committee's leadership, coordination, and engagement. Explicit charges at the Financial Condition Committee level tied to advancing the Framework present a critical opportunity to further embed its principles into the NAIC's ongoing workstreams and ensure consistent regulatory oversight.

Conclusion

In closing, Athene strongly supports the NAIC's efforts to build a more coordinated and forward-thinking RBC system. The Framework provides an invaluable opportunity to modernize the regulatory approach for insurer investments, and we commend the Committee's leadership. We urge the NAIC to remain focused on implementing the Framework's principles across all ongoing initiatives and to seize this opportunity to continue leading on a global scale.

Thank you again for the opportunity to provide input, and we look forward to further constructive dialogue as the Framework's implementation progresses.

Sincerely,



Michael Consedine
Executive Vice President
Head of US Government Relations & Regulatory Affairs

October 24, 2024

RFP #XXXX | Credit Rating Provider Due Diligence

In 2023, the National Association of Insurance Commissioners' (NAIC) Financial Condition (E) Committee introduced a Framework for Regulation of Insurer Investments – A Holistic Review that was revised and exposed for comment at the 2024 Spring National Meeting. The Executive Summary of the framework is as follows:

- Recent initiatives to address gaps in the regulatory framework for insurer investments have received much attention by a variety of stakeholders.
- While the broader commentary has included many misconceptions around these initiatives, it has also included constructive feedback with themes and observations that many regulators have shared.
- At the most basic level, the question has arisen – what is the most effective use of regulatory resources in the modern environment of insurance regulation for investments?
- The historical focus of the Securities Valuation Office (SVO) has been on risk assessment of individual securities, with filing exempt securities (FE) blindly reliant on credit rating providers (CRPs) for designations.
- The SVO currently lacks the tools to provide due diligence and assessment over the use and effectiveness of CRPs, or to conduct enterprise- or industry-wide risk analytics.
- Rather than a framework that utilizes valuable SVO resources to prioritize synthesizing CRP functions, a more effective use of those resources would be to prioritize the establishment of a robust and effective governance structure for the due diligence of CRPs.
- Further, with investment in modern risk analytics tools, the SVO could provide invaluable risk analysis capabilities to better support the risk-focused approach to supervision, at both a micro- and macro-prudential level.
- The framework provides concrete proposals envisioning a modernization of the role and capabilities of the SVO in a way that correlates with the observed shift towards more complex and asset-intensive insurer business strategies.
- The framework also provides high-level guidelines for considering consistency of capital across assets as the investment RBC initiatives move forward, recognizing the practical limitations of absolute capital parity.

Currently, risk-based capital charges that support the capital framework to identify weakly capitalized insurers, rely upon NAIC Designations as the measure of investment risk, for assets reported as bonds, as well as limited risk assessment for non-bond holdings. NAIC Designations are either provided directly by the SVO for filed securities or, for the majority of insurer investments, by a direct translation of a credit rating from a CRP for those securities that are exempt from

filing (FE). There are currently no criteria for becoming a CRP beyond being an U.S. Securities and Exchange Commission (SEC) registered NRSRO and under its regulatory authority, the SEC is unable to opine on the quality of NRSRO methodologies and ratings. As such, the NAIC “blindly” relies on the CRP ratings. There is no mechanism for overall due diligence around CRP usage, no process to assess the reasonability of a CRP’s ratings, nor an ability to challenge an individual rating for not conforming to regulator expectations of how it was determined. Based on this Framework, the NAIC is planning several workstreams to address the issues identified.

Specific to the project that will result from this Request for Proposal (RFP), the NAIC is looking for detailed quantitative and qualitative technical recommendations that would address its objectives around CRP Due Diligence:

- **Reduce/eliminate “blind” reliance on CRP ratings but retain overall utilization of CRPs ratings with the implementation of a strong due diligence framework. This framework should be extremely robust with focused resources within the NAIC in its implementation and maintenance.**
- **At the completion of work for this project there should be a quantitative and qualitative (as discussed on page 16 and 17 of this RFP) due diligence framework design and implementation plan that will permit the SVO to primarily focus on the on-going administration of this holistic due diligence process around CRP usage. That process must be vigorous and consequential (e.g. clear quantitative and qualitative parameters for CRPs utilized to provide ratings for use in assigning NAIC designations).**
- **Retain ability within the SVO to perform individualized credit assessment and utilize regulatory discretion when needed, under well-documented and governed parameters. This “backstop” should be embedded in the regulatory regime, but ideally would be rarely used if other governance is optimized.**

At this time, the NAIC is soliciting proposals from qualified third-party firms for the development of a “Credit Rating Provider (CRP) Due Diligence Framework”, and detailed quantitative and qualitative analysis that supports the full development and implementation of the framework that can be repeated periodically by regulators and staff.

A clarification and question and answer session will be held at **TBD pm Central Time, Month Day, Year**. Firms interested in submitting a proposal are encouraged to attend this WebEx session. Please click [\(link\)](#) to register.

Firms intending to respond to this RFP are asked to submit an email indicating their intent to bid and Point of Contact details by **5pm Central Time, Day, Month, Year**, via email to Jim Woody at Proposals@naic.org.

To receive consideration, final proposals must be sent electronically to Proposals@naic.org no later than **5pm Central Time, Day, Month, Year**.

Proposals must address each item described within the RFP Response Requirements: 1| Respondent Company Overview, 2| Detailed RFP Response / Proposal, 3| Additional Required Documentation, and 4| Additional Instructions.

RFP | Schedule

	RFP released
	Clarification & Q&A Session register here
	Vendor intent to Bid due to Proposals@naic.org
	Vendor RFP questions due to Proposals@naic.org
	NAIC responses to vendor questions
	Vendor submissions due by 5pm CT to Proposals@naic.org
	Vendor Interviews, if needed
	Projected Vendor Selection and RFP Award*
	Projected Project Start

* NAIC's Executive Committee has the final authority to direct contract execution for the selected vendor.

Selection Criteria

The RFP Selection Committee will base the vendor selection on criteria including:

- Completeness and quality of the proposal
- Experience with similar projects and the credit ratings process
- Professional reputation of the firm and qualifications of individuals assigned to this project
- Proposed project timeline and cost
- Analytical alignment of the proposed framework to the NAIC's financial solvency objectives.

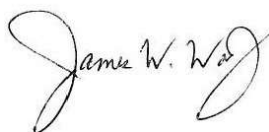
The NAIC reserves the right to reject any or all proposals, request new proposals or request additional information. The NAIC reserves the right to further negotiate with any or all bidders.

Questions

Proposal-related questions should be submitted to Proposals@naic.org by **5pm Central Time, Day, Month XX, Year**. Answers to each question submitted will be posted on the NAIC RFP website by **Day, Month, Year**.

Questions related to any other matter should be directed to NAIC Chief Financial Officer Jim Woody at JWoody@naic.org, who is the NAIC point-of-contact for this RFP.

Respectfully,



James Woody, Chief Financial Officer, National Association of Insurance Commissioners



NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS (NAIC)

Request for Proposal- #(number)

Credit Rating Provider Due Diligence Framework

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Background Information

About the NAIC

The National Association of Insurance Commissioners (NAIC) is a 501(c) (3) not-for-profit organization.

The NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories.

Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC staff supports these efforts and represents the collective views of state regulators domestically and internationally. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

Role of the VOSTF

The NAIC has determined that assessing the risk of an insurance company's investments is a ~~good~~ ~~critical starting point~~ ~~element for~~ ~~in~~ assessing that insurer's financial solvency ~~position, risk over its investments.~~ ~~Credit investment risk is one of the NAIC's branded risk classifications monitored by state solvency regulators and~~ which includes considering the credit quality for bond-type securities. The Valuation of Securities (E) Task Force (VOSTF) formulates the NAIC's policies for securities that can be assigned the NAIC's measure of investment risk, an NAIC Designation. The Task Force's policies are documented and published in the [Purposes and Procedures Manual of the NAIC Investment Analysis Office](#) (P&P Manual). The NAIC has assigned the Securities Valuation Office (SVO) and Structured Securities Group (SSG) the responsibility of carrying out the policies of the VOSTF and assigned the Task Force with the responsibility to oversee the operations of these NAIC departments. The SVO and SSG, when referred to jointly, are called the Investment Analysis Office (IAO).

SVO and SSG

The SVO and SSG are staffed by investment professionals whose careers have been dedicated to investment analysis. The analysis staff in these departments typically have over 25-years of investment experience, all have a bachelor's degree, 84% have an MBA, roughly a third are chartered financial analysts (CFA) or have some other advanced level certification or degree, and two-thirds have prior work experience at rating agencies.

The SVO conducts credit quality and investment risk assessments of securities owned by state-regulated insurance companies through insurer submissions of investment documents into the NAIC's VISION application and performs other functions such as: the administration of the filing exemption process (the NAIC's automated process for translating credit rating provider ratings into an NAIC Designation), compilation and publication of the SVO List of Investment Securities (a data set of all NAIC Designations published in the NAIC's AVS+ application), list of credit ratings eligible for translation, the list of funds eligible to receive NAIC Designations, the list of qualified

U.S. financial institutions that can issue letters of credit for reinsurance purposes, assessment of derivative counterparties, the list of sovereign NAIC Designation equivalents, and any other process mandated in the P&P Manual.

The SSG assesses the credit quality and investment risks in securitizations and other complex financially engineered securities through the utilization and oversight of external financial modeling vendors. Typically, these are residential mortgage-backed securities (RMBS), commercial mortgage-backed securities (CMBS), mortgage reference securities and, beginning in 2025, collateralized loan obligations (CLOs).

NAIC | Mission Statement

The mission of the NAIC is to assist the state insurance regulators, individually and collectively, in serving the public interest and achieving the following fundamental insurance regulatory goals in a responsive, efficient, and cost-effective manner, consistent with the wishes of its members:

- *Protect the public interest;*
- *Promote competitive markets;*
- *Facilitate the fair and equitable treatment of insurance consumers;*
- *Promote the reliability, solvency, and financial solidity of insurance institutions; and*
- *Support and improve state regulation of insurance.*

Current CRP Review Criteria and Crediting Rating Use

The Use of Credit Ratings of NRSROs in NAIC Processes

Providing Credit Rating Services to the NAIC

The NAIC uses credit ratings for a number of regulatory purposes, including, to administer the filing exempt rule. Any rating organization that has been designated a Nationally Recognized Statistical Rating Organization (NRSRO) by the U.S. Securities and Exchange Commission (SEC) and which continues to be subject to federal regulation, may apply to provide Credit Rating Services to the NAIC for the classes of credit ratings for which it is registered as an NRSRO.

Policy and Legal Disclosure Pertaining to the NAIC Credit Rating Provider (CRP) List

The NAIC uses publicly available credit ratings, when available, as one component of the services it provides to state insurance regulators concerned with financial solvency monitoring of insurance company investments.

The NAIC acts solely as a private consumer of credit ratings. The sole NAIC objective in obtaining and using credit ratings is to conserve limited regulatory resources; e.g., the resources of the SVO. The VOS/TF has established the procedure specified in this section solely to ensure that the NAIC can avail itself of credit rating opinions.

The NAIC does not select, approve or certify NRSROs or other rating organizations or distinguish among them for any public or policy purpose whatsoever. Nor does the NAIC endorse the credit rating or analytical product of any CRP or rating organization or distinguish between CRPs or rating organizations for any specific public purpose. The NAIC disclaims any authority to regulate CRPs or rating organizations.

NAIC Designations

NAIC Designations are proprietary symbols of the NAIC. The SVO, the SSG and, under certain circumstances, insurers, produce NAIC Designations for insurer-owned securities using the policies, procedures or methodologies adopted by the VOSTF in the P&P Manual. NAIC Designations are produced for statutory accounting, reporting, state investment laws and other purposes identified in the NAIC Financial Regulation Standards and Accreditation Program and/or other NAIC developed regulatory guidance embodied in state law. They must be considered in the context of their appropriateness and consistency of use in the NAIC Policy Statement and Financial Regulation Standards (SFRS) and other NAIC guidance.

NAIC Designations represent opinions of gradations of the likelihood of an insurer's timely receipt of an investment's full principal and expected interest ("investment risk"). Where appropriate for a given investment, NAIC Designations and Designation Categories shall reflect "tail risk" and/or loss given default, the position of the specific liability in the issuer's capital structure, and all other risks, except for volatility/interest rate, prepayment, extension or liquidity risk. NAIC Designations shall be identified by the NAIC 1 through NAIC 6 symbols (as

modified by NAIC Designation Categories) which indicate the highest quality (least risk) to the lowest quality (greatest risk), respectively.

Investment risk is the likelihood that an insurer will receive full and timely principal and expected interest. It differs from “credit risk” which focuses on the ability of an issuer to make payments in accordance with contractual terms. Credit risk is, at times, too narrow a concept for NAIC purposes. For example, the performance component of a principal protected security (PPS) may produce no return and, therefore, the PPS could pay no interest with no event of default by the issuer. As such, focusing solely on credit risk could limit the SVO’s ability to assess the risk of the performance component of a principal protected security or on potential risks posed by other investment types.

NAIC Designation Category – Means and refers to 20 more granular delineations of investment risk in the NAIC 1 through NAIC 6 investment risk scale used by the VOS/TF to relate investment risk in insurer-owned securities to a risk-based capital factor assigned by the NAIC Capital Adequacy (E) Task Force. Each delineation of investment risk is represented by a letter (a Modifier) which modifies the NAIC Designation grade to indicate a more granular measure of investment risk within the NAIC Designation grade. The more granular delineations of investment risk are distributed as follows: 7 for the NAIC 1 Designation grade indicated by the letters A through G; 3 delineations each for each of the NAIC Designation grades NAIC 2, NAIC 3, NAIC 4 and NAIC 5 indicated by the letters A, B and C and 1 delineation for NAIC Designation grade NAIC 6. The NAIC Designation Category framework is shown in the P&P Manual. All Modifiers roll up into the respective NAIC Designation grade as they are a subset of them.

NAIC Designation	+	NAIC Designation Modifier	=	NAIC Designation Category
1		A		1.A
1		B		1.B
1		C		1.C
1		D		1.D
1		E		1.E
1		F		1.F
1		G		1.G
2		A		2.A
2		B		2.B
2		C		2.C
3		A		3.A
3		B		3.B
3		C		3.C
4		A		4.A
4		B		4.B
4		C		4.C
5		A		5.A
5		B		5.B
5		C		5.C
6				6

An objective of the VOS/TF is to support regulators in the assessment of the financial ability of an insurer to maintain financial solvency, through the making of policy concerning insurer investment risk and the identification and sharing of pertinent information with other relevant regulators and regulatory groups responsible for the NAIC’s regulatory framework.

NAIC Policy on the use of Credit Ratings of NRSROs

Procedure to Become an NAIC Credit Rating Provider

An NRSRO that wishes to provide Credit Rating Services to the NAIC may indicate its interest by sending a letter to the Chair of the VOS/TF with a copy to the Director of the SVO, in which it:

- Indicates an interest in providing Credit Rating Services to the NAIC.
- Confirms that it is currently an NRSRO subject to regulation by the SEC.
- Provides a chart relating its credit rating symbols to NAIC Designations.
- Indicates that the NRSRO agrees to enter into a legally binding agreement under which the NRSRO will:
 - Provide Credit Rating Services to the NAIC at no cost;
 - Reimburse the NAIC for all costs associated with: integration of its data feed into NAIC systems, subsequent changes to NAIC systems to accommodate changes in the NRSRO's systems and changes to NAIC systems as a result of the termination of Credit Rating Services by the NRSRO;
 - Give written notice 6 months prior to terminating Credit Rating Services; and
 - Agree not to claim in marketing literature that the provision of Credit Rating Services indicates NAIC approval or endorsement of the NRSRO, its products or services.

When directed to do so by the VOS/TF, the SVO shall add the name of the NRSRO (thereafter described as a Credit Rating Provider (CRP)) to the NAIC Credit Rating Provider List in the publication of the P&P Manual that follows the execution of an agreement between the NAIC and the NRSRO.

Regulatory Significance – Filing Exempt Rule

Adding the name of an NRSRO to the Credit Rating Provider List indicates that insurance companies must use the credit ratings assigned by that NRSRO, if any, when determining the NAIC Designation equivalent for a security to be reported under the filing exempt rule. Only those NAIC CRP ratings that meet the definition below may be translated into NAIC Designations under the filing exempt rule. Securities assigned ratings by NAIC CRPs that do not meet the definition below, shall be filed with the SVO. The translation of a NAIC CRP rating into an NAIC Designation is conducted in accordance with the procedures described in the P&P Manual.

Definition – Credit Ratings Eligible for Translation to NAIC Designations

As disclosed below, the NAIC may determine that the rated security or investment is of a type that is not eligible to be reported on Schedule D or that the NAIC determines is not appropriate for NRSRO credit ratings to be used to determine the regulatory treatment of a specific asset class, as specified in the P&P Manual.

The credit rating of the CRP to which this section and the NAIC Credit Rating Provider List refers to is the (a) credit rating assigned by the NAIC CRP; (b) by application of a CRP's proprietary long-

term obligation ratings scale and methodology; to (c) securities.

Credit ratings of a NAIC CRP that meet this definition are entitled to a presumption of convertibility to the equivalent NAIC Designation published in the NAIC Credit Rating Provider List except that the presumption of convertibility is subject to the following limitations:

- Those rating activities or markets in which the entity has NAIC CRP status.
- Securities with monitored NAIC CRP ratings that:
 - Are monitored at least annually by the CRP that issued the rating;
 - Are assigned to a specific issue that must be specifically identified;
 - Apply to securities where the issuer promises to repay principal and interest or dividends;
 - Convey an opinion as to the likelihood of payment of both principal and interest/dividends due from the issuer to the holders of the security; or
 - Are structured to pay only principal or only interest/dividends, if the monitored NAIC CRP rating addresses the likelihood of payment of either the principal, in the case of a security structured to pay only principal or the interest/dividends, in the case of security structured to pay only interest/dividends (an “Eligible NAIC CRP Rating”).

Special Rating Systems

Unless otherwise specifically approved by the VOS/TF special rating systems of any CRP, rating agency or rating organization shall not be entitled to a presumption of convertibility. Nevertheless, an SVO analyst assessing a security that has been assigned such a rating by any rating organization, including a CRP, may consider the information imparted by that rating or a related research report as one factor in determining an NAIC Designation

List of NAIC Credit Rating Provider

The CRPs that provide Credit Rating Services to the NAIC are (listed alphabetically):

- A.M. Best Rating Services, Inc. (A.M. Best) – For credit ratings issued to insurance companies; corporate issuers and issuers of asset-backed securities.
- DBRS, Inc. (DBRS Morningstar) – For credit ratings issued to financial institutions, brokers, or dealers; insurance companies; corporate issuers; issuers of asset-backed securities and issuers of government securities, municipal securities, or securities issued by a foreign government.
- Egan-Jones Ratings Co. – For credit ratings issued to financial institutions, brokers, or dealers; insurance companies and corporate issuers.
- Fitch Ratings, Inc. – For credit ratings issued to financial institutions, brokers, or dealers; insurance companies; corporate issuers; issuers of asset-backed securities and issuers of government securities, municipal securities, or securities issued by a foreign government.
- HR Ratings de Mexico, S.A. de C.V. – For credit ratings issued to financial institutions, brokers, or dealers; corporate issuers and issuers of government securities, municipal securities, or securities issued by a foreign government.
- Kroll Bond Rating Agency, LLC. – For credit ratings issued to financial institutions, brokers,

or dealers; insurance companies; corporate issuers; issuers of asset-backed securities and issuers of government securities, municipal securities, or securities issued by a foreign government.

- Moody's Investors Service, Inc. for credit ratings issued to financial institutions, brokers, or dealers; insurance companies; corporate issuers; issuers of asset-backed securities and issuers of government securities, municipal securities, or securities issued by a foreign government.
- S&P Global Ratings, for credit ratings issued to financial institutions, brokers, or dealers; insurance companies; corporate issuers; issuers of asset-backed securities and issuers of government securities, municipal securities, or securities issued by a foreign government.

The Credit Rating Providers identified above include those of its affiliates that the credit rating provider identified to the U.S. Securities and Exchange Commission (SEC) as part of its Form NRSRO Application as a separate legal entity or a separately identifiable department or division of the credit rating provider that determines credit ratings that are credit ratings of the credit rating provider and which the SEC treats as a credit rating issued by the credit rating provider for purposes of Section 15E of the Exchange Act and the SEC's rules thereunder. The full list of CRP ratings eligible for translation to an NAIC Designation can be found on the SVO's webpage: [NAIC – Credit Ratings Eligible for Translation to NAIC Designations](#).

CRP Credit Rating Equivalent to NAIC Designations and NAIC Designation Categories
(agencies listed in order as they appear in the P&P Manual)

			Credit Rating Providers (*) (Pursuant to the guidance in this Manual; particularly, Part One, "The Use of Credit Ratings of NRSROs in NAIC Processes," "Filing Exemptions," "Policies Applicable to Specific Asset Classes," and Part Three, "Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities")							
NAIC Designation	NAIC Designation Modifier	NAIC Designation Category	Moody's Investors Service, Inc.	S&P Global Ratings	Fitch Ratings, Inc.	DBRS, Inc. (DBRS Morningstar)	A.M. Best Rating Services, Inc.	Kroll Bond Rating Agency, LLC	Egan-Jones Ratings Co.	HR Ratings de Mexico, S.A. de C.V.
1	A	1.A	Aaa	AAA	AAApr, AAA	AAA, Pfd-1 (high)	aaa	AAA	AAA	HR AAA (G)
1	B	1.B	Aa1	AA+	AA+	AA (high), Pfd-1	aa+	AA+	AA+	HR AA+ (G)
1	C	1.C	Aa2	AA	AA	AA, Pfd-1 (low)	aa	AA	AA	HR AA (G)
1	D	1.D	Aa3	AA-	AA-	AA (low), Pfd-1	aa-	AA-	AA-	HR AA- (G)
1	E	1.E	A1	A+	A+	A (high)	a+	A+	A+	HR A+ (G)
1	F	1.F	A2	A	A	A	a	A	A	HR A (G)
1	G	1.G	A3	A-	A-	A (low)	a-	A-	A-	HR A- (G)
2	A	2.A	Baa1	BBB+	BBB+	BBB (high), Pfd-2 (high)	bbb+	BBB+	BBB+	HR BBB+ (G)
2	B	2.B	Baa2	BBB	BBB	BBB, Pfd-2	bbb	BBB	BBB	HR BBB (G)
2	C	2.C	Baa3	BBB-	BBB-	BBB (low), Pfd-2 (low)	bbb-	BBB-	BBB-	HR BBB- (G)
3	A	3.A	Ba1	BB+	BB+	BB (high), Pfd-3 (high)	bb+	BB+	BB+	HR BB+ (G)
3	B	3.B	Ba2	BB	BB	BB, Pfd-3	bb	BB	BB	HR BB (G)
3	C	3.C	Ba3	BB-	BB-	BB (low), Pfd-3 (low)	bb-	BB-	BB-	HR BB- (G)
4	A	4.A	B1	B+	B+	B (high), Pfd-4 (high)	b+	B+	B+	HR B+ (G)
4	B	4.B	B2	B	B	B, Pfd-4	b	B	B	HR B (G)
4	C	4.C	B3	B-	B-	B (low), Pfd-4 (low)	b-	B-	B-	HR B- (G)
5	A	5.A	Caa1	CCC+	CCC+	CCC (high), Pfd-5 (high)	ccc+	CCC+	CCC+	HR C+ (G)
5	B	5.B	Caa2	CCC	CCC	CCC, Pfd-5	ccc	CCC	CCC	HR C (G)
5	C	5.C	Caa3	CCC-	CCC-	CCC (low), Pfd-5 (low)	ccc-	CCC-	CCC-	HR C- (G)
6	6	6	Ca	CC	CC	CC (high)	cc	CC	CC	HR D (G)
6	6	6	C	C	C	C	c	C	C	
6	6	6		D	DD	CC (low)	d	D	D	
6	6	6			DD	C (high)				
6	6	6			D	C				
6	6	6				C (low)				
6	6	6				D				

Note: * This is a listing of only the "generic" Credit Rating Provider (CRP) rating symbols. CRPs use a variety of symbols; including, combinations of prefixes and suffixes that provide additional information about the rating symbol which are described in the CRP's documentation. There are over 2,000+ unique rating symbols used by CRPs to describe long-term securities. The SVO webpage (<https://www.naic.org/svo.htm>) maintains a master list of Credit Ratings Eligible for Translation to NAIC Designations. The SVO does not currently translate short-term security ratings as part of its Compilation and Publication of the SVO List of Investment Securities incorporated into the NAIC's AVS+ product.

Credit Rating Provider Due Diligence Objectives

Vision and Objectives

Specific to the project that will result from this Request for Proposal (RFP), the NAIC is looking for detailed quantitative and qualitative technical recommendations that would address its objectives around CRP Due Diligence:

- Reduce/eliminate “blind” reliance on CRP ratings but retain overall utilization of CRPs ratings with the implementation of a strong due diligence framework. This framework should be extremely robust with focused resources within the NAIC in its implementation and maintenance.
- At the completion of work for this project there should be a quantitative and qualitative due diligence framework design and implementation plan that will permit the SVO to primarily focus on the on-going administration of this holistic due diligence process around CRP usage. That process must be vigorous and consequential (e.g. clear quantitative and qualitative parameters for CRPs utilized to provide ratings for use in assigning NAIC designations).
- Retain ability within the SVO to perform individualized credit assessment and utilize regulatory discretion when needed, under well-documented and governed parameters. This “backstop” should be embedded in the regulatory regime, but ideally would be rarely used if other governance is optimized.
- ~~Quantitative and qualitative analysis, both initial and ongoing, should be applied to all CRPs and CRP applicants consistently and equally. State regulators and the NAIC are agnostic to the credit rating providers used in the NAIC Designation process, subject to the due diligence framework as established.~~

The request also includes some aspects of other components of our framework, when impactful to the objectives above. This includes recommendations of how to best utilize and enhance the structured asset modeling capabilities of the SVO and for recommended governance and oversight of the SVO’s operations (i.e. the production and oversight of NAIC designations.)

This project should be delivered in two phases. Phase 1 deliverables include recommendations and considerations on how to accomplish the objectives, with consideration to the questions below, and Phase 2 Deliverables will include development of the recommendations into an actionable framework for the NAIC to implement and maintain.

The following guidance should inform the approach to addressing the objectives above:

- Quantitative and qualitative analysis, both initial and ongoing, should be applied to all CRPs and CRP applicants consistently and equally. State regulators and the NAIC are agnostic to the credit rating providers used in the NAIC Designation process, subject to the due diligence framework as established. Accordingly, the process should not encourage a uniformity of thought among the CRPs.
- The scope is all existing CRPs and future CRP applicants (with the intent of “reapplication” periods on a periodic basis)

- The ultimate design of the due diligence framework will be decided through the established policies and procedures of the NAIC and is expected to leverage the recommendations made by the selected vendor. The goal is to be as transparent through the process as possible while balancing any sensitivity of the selected vendor to details of its report being made public. Regardless of the degree to which vendor recommendations can be made public, the ultimate design of the due diligence framework and the justification for such will be attributable to the NAIC and its state regulator members and subject to the open, transparent processes of the NAIC whereby all stakeholders will have the opportunity to provide input.
- The ultimate design of the due diligence framework should also target the highest degree of transparency possible on an ongoing basis, with the express intention of fostering stability and predictability for all stakeholders in balance with meeting the regulatory objectives of the framework.
- NAIC will have responsibility to implement and maintain the ultimate framework under the oversight of state regulators.
- A specific timeline has not been determined for this project and vendors should provide their own anticipated timeline. It is understood that Phase 2 timelines are based on the outcomes of Phase 1 and will be less firm.
- The ultimate approach should be designed in such a way that it can evolve naturally with capital markets and innovation, without penalizing new and emerging asset types.
- While the following sections provide many questions for consideration, the process, sources and deliverables are deliberately left open-ended, and proposed solutions with characteristics not considered within this document are welcome.

Quantitative Analysis

Currently, NRSROs applying to be a CRP provide their own mapping of NRSRO ratings to corresponding NAIC Designations. The NAIC would like to be able to utilize data in order to validate this mapping and/or establish its own mapping. A key objective is that ratings performance is shown to be representative of those used specifically for NAIC Designations (rather than all ratings issued by an NRSRO, if not otherwise representative of those used for NAIC Designations). For that purpose:

- What analytical approach should be used to compare each rating agency's rating methodology for a given security type, or sector/industry, or more broadly, to use those ratings to map and assign NAIC Designations?;
- How should jointly-rated -securities (rated by more than one rating agency) and single-rated securities be analyzed? Should they be analyzed and mapped differently?
- Should public credit ratings and a private credit ratings be distinguished for quantitative analysis purposes analysis and mapping purposes?;
- Should ratings on securities from only one CRP be analyzed and mapped differently? Should the NAIC consider requiring two or more ratings to inform a designation to reduce reliance on a single rating?
- For securitizations, should ratings be analyzed and mapped differently if different CRPs

are rating different tranches in a single securitization (i.e. no consistent CRP throughout the securitization)?

- How should ratings that incorporate a security's expected loss given default (versus simple probability of default) impact the analysis and mapping?
- What is the scope of the **assessment analysis and mapping**, i.e. at a rating agency level, or at an asset-class, sector or other specified basis?
- Should analysis be heavily weighted toward default and loss experience associated with rating levels? NRSROs have noted default studies may not be sufficient for investment grade portions of rating scales, whereas non-investment grade ratings may have higher rates of transition and default. What other metrics could be utilized for analysis and mapping?
- How should the analysis consider economic or financial market conditions over the periods covered, particularly periods of extreme distress for credit such as the Global Financial Crisis, dotcom bubble, junk bond crash, S&L crisis, OPEC oil embargo, or any other major bond market distress event?
- To what extent can the NAIC rely on market usage of ratings to act as a validating tool, and how does that apply to private ratings that are not issued publicly?
- How would the analysis demonstrate that the credit ratings can be used as a proxy for an NAIC Designations?
- How should new investment types, emerging asset classes without quantifiable history, newly established NRSROs, etc. be considered when applying the ultimate framework?

Sources of Data

- What specific fields and definitions would you need from the CRP applicant, the frequency of the observations and the elapsed time period in years or date ranges?
- Are NRSRO filings with the U.S. Securities and Exchange Commission sufficient for this analysis and how? How can we ensure this data is aligned with the ratings most predominantly used in the NAIC designation process (for example, solicited versus unsolicited ratings)?
- Could this analysis be best performed utilizing the NAIC's own data, presumably best reflective of insurer's actual investment universe, and if so, how could that ~~should~~ be accomplished most effectively?
- Should data be required of the insurance companies themselves, including internal rating assessments, given insurers have the ultimate responsibility for prudent investment oversight? What potential enhancements to governance procedures applicable to insurers and insurance groups be considered in their use of CRP ratings?
- How could the state insurance supervisory examination process provide information or data to inform the analysis and mapping?
- The NAIC's Structured Securities Group ("SSG") has modeling capabilities, both current and planned, meant to assess the growing structured securities market. How should those capabilities be used to monitor the rating agency ratings on structured securities? What enhancements that can be made to those capabilities to further utilize them effectively?
- What other sources of data would be most beneficial to this process? Preference should be given to data that is most easily obtained. This may require collaboration with NAIC staff, industry and NRSROs to identify.

- NOTE: Dependent on data sources identified, the NAIC will retain responsibility for control of data and data access as well as appropriate cyber hygiene principals for data storage and administration.

Other Considerations for CRP Qualifications

- What procedures and policies should be implemented to facilitate ~~periodic, and periodic,~~ and transparent discussions between the NAIC, regulators and CRPs regarding NAIC's use of ratings, as a consumer, in its regulatory framework, including emerging investments & methodologies, questions NAIC may have on existing investments, discussions the CRPs wish to have with the NAIC, etc? Additionally, what safeguards should be put in place to ensure that the NAIC does not violate the Credit Rating Agency Reform Act?
- What is the overarching process for how the NAIC should implement a review process? Initial application, renewal application (what time frame), upon certain triggers such as SEC Violations or other legal actions?
- What are the qualifications that a rating agency should possess to be an input into the NAIC designation process, and how the NAIC should assess those qualifications?
- What should disqualify a rating agency from being a CRP to the NAIC?
- What are any actual, potential or potentially perceived conflicts of interest that should disqualify a rating agency from being a CRP to the NAIC, including measurable items such as material relationships with insurers or their ownership entity. How should conflicts of interest be defined for this purpose and how should they be disclosed to the NAIC?
- SEC Violations or other legal actions and how to assess.
 - If a CRP was to be disqualified based on criteria established, what steps should it take to remediate this at a firm, asset-class, sector or other level.

Ongoing review internal oversight

- Define an examination/review process state regulators can utilize to provide oversight of the SVO in its implementation of this framework, along with its own production of designations and its usage of individualized challenges to CRP ratings in the designation process.
- Define an examination/review process state regulators can utilize to provide oversight of the SSG in its implementation of this framework, its own production of modeling-based designations (both internally and outsourced), including model governance and validation.
- While overall processes would be internally performed, aid in the design an informative report that can be provided at the relevant NAIC committee(s) to demonstrate such oversight to interested parties and other market participants.
- Define an examination/review process state regulators and the NAIC can utilize to regularly reassess this framework, and the mapping and assignment of NAIC Designations to enhance consistency of the due diligence framework.

RFP Response Requirements

Required Sections and Information

Respondents to this RFP are asked to include the following sections and information in their submitted proposals:

- | **Respondent Company Overview**

- Concise description and overview of the company and its history.
- Outline of services the company offers, as it relates to requirements outlined in this RFP.
- A brief history and description of any work carried out for NAIC or any NRSRO in the last ten (10) years.
- A brief history and description of delivery of projects of this or similar type.
- A description of the company's familiarity with the state-based insurance regulatory framework and the role of the NAIC, including the Securities Valuation Office.
- A description of the company's familiarity with NAIC designations and how they are utilized in the regulatory framework, including for purposes of applying risk-based capital charges to insures to identify weakly capitalized companies.
- A description of the company's knowledge of credit ratings and credit rating agencies, including measurements of performance and default studies, or a description of the company's access to such information.
- A detailed description of the capabilities and experience of the company to perform the requirements of the project contemplated by this RFP, including experience evaluating data in a complex environment
- Details of the point of contact who will facilitate this project, their biography, experience, and contact information.
- Biographies of key personnel to be assigned to this project, including their role and specific experience and expertise.
- Detailed description of three to five similar engagements completed, noting projection duration and total cost, and a client reference for each.
- Disclose in detail any actual, potential or potentially perceived conflicts of interest of your firm or anyone working on this initiative may have analyzing rating agencies, issuers of securities with ratings (public or private) or investors in securities with ratings (public or private). Note it is recognized that these types of relationships will normally occur in concert with the familiarity and expertise this initiative requires, and that any actual, potential, or potentially perceived conflicts of interest will not automatically disqualify your firm or anyone working on this initiative.
- Any other information that the respondent feels relevant / useful as it pertains to the requirements outlined in this RFP.

• | Detailed RFP Response / Proposal

Respondents should prepare a detailed RFP response / proposal that addresses the objectives of the preceding section, including:

- A detailed narrative on how you anticipate approaching this project*
- What methodology(ies) you will utilize
- What data sources you will utilize
- What resources you will require from the NAIC, SVO and regulators
- Any initial conclusions or recommendations regarding the outcome of this project

*The first item above (approach to project) is considered the most important aspect of the respondent's proposal. Please consider this in your proposal as well as how the approach incorporates the methodology and data sources.

Project Plans

Project plans for completion of the analysis outlined in this RFP, that include, to a reasonable amount of detail:

- Key tasks, activities, milestones, and deliverables.
- Relevant timelines, schedules, and input / decision points.
- Any critical assumptions and / or dependencies.

Acceptable formats for the project plans include MS Project and MS Excel.

Analysis Approach

Additional detail and relevant supporting information on the proposed software or analytical tools and processes to be used within the development of the CRP Due Diligence framework and how they relate to and impact the proposed Project Plan, Resource Plan, and Budget and Contingency Plans.

Resources Plan

Detailed resource plans to deliver the CRP Due Diligence framework, as outlined in this RFP, that include, to a reasonable amount of detail:

- Resources (both vendor and NAIC) required.
- Hours per week, by resource (both vendor and NAIC).
- Location (on-shore, off-shore) of vendor resources.
- Rates (costs per hour) of vendor resources.

The resources plans should align to the project plans (in terms of key activities, milestones,

and deliverables) and the fee schedule / pricing information.

DRAFT

Fee Schedule and Pricing Information

Detailed fee schedules, total projected budgets, and other pricing information for phase, including assumptions on:

- Additional Expenses (e.g., travel, lodging, meals, etc.)
- Technology costs (e.g., hardware, software licensing, etc.) to set up and maintain the CRP Due Diligence framework .
- Key Milestones and Deliverables (and how they relate to payment phasing).
- Recommended financial contingency provisions.

The NAIC will consider both fixed-fee and “time and materials” bids for development of the CRP Due Diligence framework.

Project Management

A detailed explanation of the project management tools, processes, and approaches to be used on the project, including:

- How vendor resources will integrate with NAIC resources.
- A communication plan (including key tasks, activities, milestones, resources needed, etc.) for the project explaining how key stakeholders will be engaged and kept updated on progress to date, hours / budget vs. plan, issues, and input and decisions needed, etc.
- A change management plan (including key tasks, activities, milestones, resources needed, etc.) for the project explaining how effective change will be delivered across all stakeholders to ensure the long-term success of the modernized CRP Due Diligence framework.
- Project governance considerations.
- A project risk assessment and risk management plan.

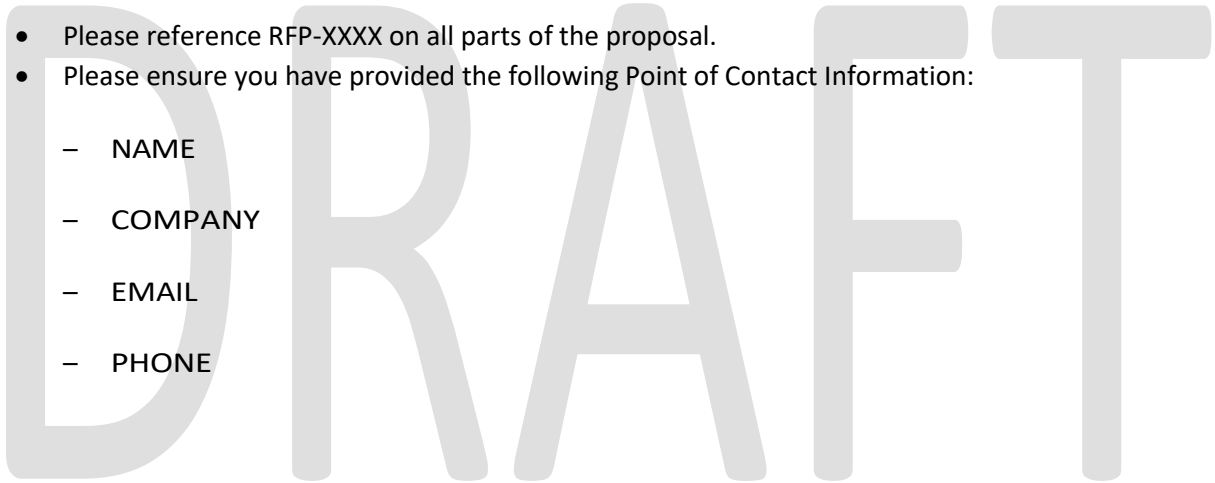
- | **Additional Required Documentation**

Respondents must provide the following information as part of their proposal:

- W-9 Form.
- Certificate of Insurance for Worker’s Compensation.
- Certificate of Insurance for Professional Liability.
- Certificate of Insurance for Cybersecurity.
- Signed NAIC Conflict of Interest Form (see Appendix 1).
- Vendor Standard Terms and Conditions (if you do not agree to, or if they vary from the NAIC Standard Terms and Conditions, see Appendix 2).

- | **Additional Instructions**

- Please reference RFP-XXXX on all parts of the proposal.
- Please ensure you have provided the following Point of Contact Information:
 - NAME
 - COMPANY
 - EMAIL
 - PHONE



RFP XXXX | Proposal Submission and Provisional Timeline

Proposal Submission

Proposals must be received by 5pm Central time on May 15, 2024, via email to Jim Woody at Proposals@naic.org.

RFP Provisional Timeline

	ACTIVITY	DATE
1	NAIC Issuance of RFP	
2	NAIC public posting of RFP on website + press release	
3	NAIC hosted project clarification & Q&A Session register here	
4	Vendor intent to Bid due to Proposals@naic.org ⁷	
5	Vendor RFP questions due to Proposals@naic.org ⁸	
6	NAIC responses to vendor questions ⁹	
7	Vendor proposal submissions due to Proposals@naic.org	
8	NAIC notice of selection for vendor interview ¹⁰	
9	Vendor Interviews	
10	NAIC issuance of award to the selected vendor - projected	
	Projected Project Start Date	

The NAIC reserves the right to change or alter timing and activities as appropriate.

* NAIC's Executive Committee has the final authority to direct contract execution for the selected vendor.

Point of Contact

Any questions regarding the requirements outlined in the RFP should be directed to Proposals@naic.org by Month, Day, Year.

Questions related to any other matter should be directed to NAIC Chief Financial Officer Jim Woody at JWoody@naic.org, who is the NAIC point-of-contact for this RFP.

⁷ Potential respondents are asked to submit an email indicating their intent to bid by Month, Day, Year mail to Jim Woody at Proposals@naic.org.

⁸ Each respondent is asked to send a single set of questions (vs. multiple sets of questions) related to RFP and response requirements.

⁹ Submitted questions will be anonymized and responses to all questions will be posted to the NAIC website.

¹⁰ The NAIC reserves the right to interview a limited number of bidders based on its evaluation of the submitted proposals. Submission of a proposal does not guarantee an interview.

Selection Process and Assessment Criteria

Selection Process

A committee including NAIC senior leadership has been designated to review the proposals, interview selected bidders, and, if appropriate, select a vendor to complete the scope of work outlined in this RFP.

This committee will also conduct regular progress meetings with the selected firm during the development and demonstration of the Proof of Concept, and during the Mobilization Planning phase.

Assessment Criteria

The following factors will be considered in making the vendor selection:

- Knowledge and understanding of NAIC systems, processes, and organization.
- Knowledge of the specific requirements and ability to understand the project.
- Experience with similar projects.
- Qualifications of staff dedicated to project.
- Professional reputation of the firm.
- Proposed project costs and timelines.
- Quality of project plans.
- Completeness of proposal.
- Proven ability to provide the identified deliverables on time and within budget.

Presentations

Based on responses, NAIC reserves the right to request a presentation of the RFP response and demonstration of capabilities included in the RFP response document.

Presentations are currently scheduled to take place from Month, Day through Month, Day, Year.

Conflicts of Interest

The NAIC recognizes that, given the broad scope of this project, any vendor with the experience reasonably necessary to produce the work may have certain conflicts of interest based upon past associations with regulators or industry participants.

These conflicts of interest will not automatically disqualify the vendor, but the vendor must have verifiable policies and procedures in place designed in compliance with established industry standards to address conflict-of-interest issues that may arise.

All relevant items must be approved prior to contract execution by NAIC's Acting Chief Executive Officer/COO/CLO.

NAIC Reserved Rights

The submission of a proposal does not guarantee an interview with the selection committee or a demonstration of capabilities to the committee.

The NAIC reserves the right to reject any or all proposals, request new proposals, or request additional information.

NAIC also reserves the right to further negotiate with any or all bidders.

The NAIC also reserves the right not to award a contract for this project.

Reasons for not awarding a contract could include, but are not limited to:

- Lack of acceptable proposals.
- An inability to come to terms with a vendor.
- A finding that insufficient funds are available to proceed.

The NAIC also reserves the right to redirect the project as is deemed advisable.

The NAIC also reserves the right to cancel this RFP at the direction of its membership.

APPENDICES

Appendix 1	NAIC Conflict of Interest Form
Appendix 2	NAIC Standard Terms and Conditions

DRAFT

Appendix 1 | NAIC Conflict of Interest Form

Any Entity that desires to contract with the NAIC must complete this form, including suppliers, consultants and purchasers of goods or services. All potential conflicts must be disclosed and approved before contract execution.

CERTIFICATION

- _____ (“Entity”) did not provide gifts, favors, membership points or any other benefits to any employee or representative of the NAIC to affect the bidding and selection process for this contract.
- Entity did not and will not receive gifts, favors, membership points or any other benefits from any employee or representative of the NAIC in connection with the negotiation or implementation of this contract.
- Entity owners, principals and employees negotiating or implementing this contract on behalf of Entity are not former NAIC employees unless disclosed below.
- Entity owners, principals and employees negotiating or implementing this contract on behalf of Entity are not immediate family members of NAIC employees unless disclosed below.

The signatory below is a duly authorized representative of Entity and hereby certifies to the authenticity and veracity of this disclosure.

Authorized Entity Signature

Date

Print Name & Company Name

DISCLOSURE

DISCLOSURE OF POTENTIAL CONFLICT

.....
.....
.....

NAIC CEO or COO

Date

Appendix 2 | NAIC Terms/Conditions

TERMS AND CONDITIONS

1. **SERVICES/CONSULTANT OBLIGATIONS**

Consultant shall provide certain consulting services to the NAIC as outlined in any Statement of Work specifically referencing this Agreement and attached hereto as Exhibit A. (detail the services the consultant will perform in a Statement of Work and attach to this agreement as Exhibit A). Consultant may perform such other services as requested by the NAIC, subject to further agreement by the Parties. Consultant shall comply with all provisions in the NAIC's Contingent Worker Policies, receipt and review of which are expressly acknowledged by Consultant. Consultant shall comply with all applicable security and safety requirements of the NAIC and shall take such training as required by the NAIC.

2. **NAIC'S AUTHORITY**

Consultant shall report directly to (indicate person and/or committee) of the NAIC for matters related to the scope of work of this Agreement, and to indicate person and/or committee) of the NAIC for administrative matters and to such other person(s) as designated. Consultant agrees to perform services required under this Agreement in compliance with the instructions and policies set forth by the NAIC. The NAIC maintains the right and authority to control Consultant's work results but will not control the means and the manner which Consultant utilizes in the attainment thereof.

3. **CONSULTANT'S AUTHORITY/INDEPENDENT CONTRACTOR STATUS**

The term "Consultant" as used in this Agreement, shall mean the individual Consultant Company and the employees or agents of the Consultant Company. The consultant is not an employee or agent of the NAIC. Consultant acknowledges that the Consultant is an independent contractor and is not authorized to act on behalf of the

NAIC. Nothing in this Agreement shall be deemed to create an agency, joint venture, partnership or franchise relationship between the Parties. Consultant shall have no authority to represent the NAIC in any hearings, negotiations or discussions, or to bind the NAIC to any contract or agreement, unless the NAIC Chief Executive Officer or NAIC Chief Operating Officer expressly and specifically gives such authority in advance and in writing.

4. **TERM**

The term of this Agreement shall begin (beginning date) and end on (end date). The Parties may extend the term by written mutual agreement. In the event that the term of a Statement of Work extends beyond the termination of this Agreement, then this Agreement shall be automatically extended for the duration of the term of such a Statement of Work.

5. **TERMINATION**

Consultant's retention and status as Consultant to the NAIC shall be terminated: Automatically on the death or dissolution of Consultant; or Automatically, upon Consultant becoming physically or mentally disabled or otherwise incapacitated in some manner which prevents the full performance of duties under this Agreement; or thirty (30) days after either the NAIC or Consultant receives written notice from the other Party of intention to terminate this Agreement. No cause need be specified by either Party for the termination.

6. **BACKGROUND CHECKS**

All Consultants performing work under this Agreement either onsite or by accessing NAIC systems remotely shall be subject to background checks, including but not limited to criminal background checks. The background checks shall be provided by the Consultant Company upon agreement with the NAIC as to form and substance for any Consultants performing under this Agreement provided such checks are completed no sooner than one (1) year prior to the Consultant beginning work under this agreement. The Consultant Company shall send the background check results to the NAIC People Operations and Engagement's Employee Engagement Coordinator. In the event the individual Consultant's Company refuses to provide a copy of the background check results, a letter from the Consultant Company to

the NAIC may be substituted. Such letter must indicate that a criminal records history search has been completed (which covers federal, state and county searches) within the last year for the individual Consultant and the results did not contain any of the following notations: i.) being found on the National Sex Offender Registry; ii.) Having a misdemeanor conviction for any of the following: illegal use/possession of weapons/explosives; violence, domestic violence, assault, battery, arson, resisting police; sex crimes including stalking, indecent exposure, prostitution, rape, sexual assault, harassment; theft, robbery, burglary, embezzlement, fraud, larceny, forgery, dishonesty; computer crimes, hacking, software infringement; iii.) Any felony convictions. In the event Consultant is unable to provide the NAIC with a background check, and upon the NAIC's agreement, the NAIC will conduct the background check. For background checks conducted by the NAIC or its assigns, all Consultants agree they will complete all necessary documents to complete the checks, including but not limited to waivers, requests for information which may include but is not limited to information regarding date of birth, social security number or driver's license number, work history, or other such documents as may be requested.

7. **COMPENSATION AND BENEFITS**

Consultant shall be paid (indicate amount(s) and methods of payment). This compensation shall be paid (indicate timing of payments) and upon presentation of a bill and approval by the NAIC that all services have been provided by the Consultant. Consultant shall not be on the regular NAIC payroll. Consultant shall not receive any NAIC employee benefits, including but not limited to medical health insurance, long-term disability insurance, group life insurance, and vacation benefits, even if Consultant is retroactively or otherwise classified as a NAIC employee for any purpose. The NAIC shall not deduct, withhold or pay taxes on the amounts paid to Consultant. Consultant shall be solely responsible for any and all tax obligations of the Consultant arising from or relating to this Agreement, including but not limited to all city, state and federal income taxes, social security withholding tax and other self-employment tax incurred by the Consultant,

and shall indemnify and hold harmless the NAIC against any liabilities, costs and expenses suffered or incurred by the NAIC as a result of any determination by the Internal Revenue Service or any other taxing or other authority that any Consultant is an employee of the NAIC.

8. **EXPENSES**

The NAIC shall pay reasonable and necessary expenses incurred by Consultant, including reasonable travel and travel-related expenses, provided the NAIC has approved such travel in writing prior to the date of travel. The NAIC shall not be obligated to pay for travel or travel-related expenses not approved in writing by the NAIC prior to the date of travel. In incurring and submitting expenses, Consultant shall comply with the NAIC's guidelines defining authorized expenses and proper documentation of expenses as set forth in the NAIC's Guidelines for Reimbursement of NAIC Travel Expenses). Within ten (10) days after Consultant completes the travel, Consultant shall submit an invoice with appropriate documentation to the NAIC.

9. **CONFIDENTIALITY OF INFORMATION AND REGULATORY SECRETS OF THE NAIC AND STATE INSURANCE DEPARTMENTS**

Except as otherwise provided herein, each Party expressly undertakes to retain in confidence all information and know-how transmitted to the other that the disclosing party has identified as being proprietary and/or confidential or, by the nature of the circumstances surrounding the disclosure, ought in good faith to be treated as proprietary and/or confidential, and expressly undertakes to make no use of such information and know-how except under the terms and during the existence of this Agreement. However, neither Party shall have an obligation to maintain the confidentiality of information: (i) received rightfully from a third party prior to its receipt from the disclosing party; (ii) the disclosing party has disclosed to a third party without any obligation to maintain such information in confidence; or (iii) independently developed by the obligated party. Further, either Party may disclose confidential information as required by governmental or judicial order, provided such Party gives the other Party prompt written notice prior to such disclosure and complies with any protective order (or equivalent) imposed on such disclosure.

In addition to the foregoing, Consultant shall treat all NAIC, NIPR and state insurance department information including but not limited to source codes, design architecture, product adaptation materials, marketing strategies, customer lists, financial

information, state data, trade secrets and unpublished information,

as confidential information and shall not disclose, disseminate, or distribute such materials to any third party without the NAIC's prior written permission. Notwithstanding this prohibition, Consultant shall not be held criminally or civilly liable for disclosing trade secret information when such disclosure is made in confidence to a federal, state or local governmental official or to an attorney for the sole purpose of reporting or investigating a suspect violation of law or is made in a complaint or other document filed in a lawsuit or other proceeding if such filing is made under seal. Each Party's obligation under this Section shall not continue if the information protected hereby falls into the public domain through no fault of the obligated Party.

Failure to comply with this Section shall constitute a material breach of this Agreement and the Agreement may be terminated as a result.

10. **CONFLICT OF INTEREST**

In the interest of fulfilling the objectives and goals of the NAIC even the appearance of impropriety must be avoided. Therefore, Consultant shall not have, and by executing this Agreement warrants it does not have, any interest with or adverse to the NAIC, any state insurance department, or NAIC member, including representation of clients or himself/herself in matters before any department, or NAIC member, regardless of capacity, or other relations with the NAIC, a state department or NAIC member as to create a conflict of interest or the appearance of such.

Consultant acknowledges it has reviewed the Conflict of Interest Policy of the NAIC and certifies no such conflict exists, except as may be disclosed. The Consultant shall complete the NAIC CONFLICT OF INTEREST FORM. If a conflict is disclosed prior to or during the term of this Agreement, the Chief Executive Officer or Chief Operating Officer of the NAIC shall review the conflict and may waive the conflict upon proper documentation or as otherwise may be appropriate.

11. **OWNERSHIP OF WORK PRODUCT**

Consultant and its personnel will be expected to do creative work that may lead to inventions, discoveries, developments, modifications, procedures, ideas, innovations, systems, programs, know-how, literary properties, or other work products (collectively the "Work Product"). Consultant agrees that the Work Product of Consultant and its personnel during their work for the NAIC shall be the sole and exclusive property of the NAIC. Consultant and its personnel hereby irrevocably assign to the NAIC all rights to the Work Product. To the extent that any such Work Product is copyrightable, it shall be deemed to be a "work for hire" within the meaning of the Copyright Law. Consideration for such assignment is hereby acknowledged. The NAIC may, at its discretion, affix such notices and take such steps as it deems reasonably appropriate to secure and perfect copyright protection in the Work Product anywhere in the world. Consultant also acknowledges any other intellectual property rights in the Work Product, including trademark, belong solely to the NAIC. Consultant and its personnel shall take all such further steps as may be reasonably requested by the NAIC to perfect the NAIC's sole and exclusive ownership of the Work Product.

12. **PUBLICITY**

Consultant agrees not to use the name of the National Association of Insurance Commissioners or the term "NAIC" in any form or attribution in connection with any solicitation, publicity, advertising, endorsement or other promotion without the express prior written permission of the NAIC.

13. **INSURANCE COVERAGE**

Consultant shall procure and maintain, at its own expense, Comprehensive General Liability coverage and Umbrella and/or Excess Liability coverage with minimum total limits of \$2,000,000 combined and \$1,000,000 single event limit for property damage and bodily injury. [Next sentence - If applicable] Consultant shall maintain cyber insurance coverage in the amount of \$1,000,000 as related to the scope of work anticipated by this agreement. Consultant shall procure and maintain for itself and its employees all insurance coverage required by federal, state or local law, including Workers' Compensation insurance and a minimum of \$500,000 in Employer's Liability coverage. Consultant shall name the NAIC as additional insured, as respects this particular Agreement in its Comprehensive General Liability and Umbrella and/or Excess Liability coverage. Consultant shall furnish to the NAIC Certificates of Insurance evidencing all of the above-required coverages and naming the NAIC as

additional insured as required. Said certificate(s) shall contain a provision whereby thirty (30) days' notice must be received by the NAIC prior to cancellation, termination or a material change in coverage by either Consultant or Insurer.

Consultant shall provide or offer to provide minimum essential health care coverage (as defined in the Affordable Care Act and the associated Internal Revenue Code and regulations) for any individual Consultant placed at the NAIC.

14. INDEMNIFICATION

Consultant hereby agrees to defend, indemnify and hold harmless the NAIC, its successors and parents, subsidiaries and affiliates and their employees, officers, directors and members, from and against any loss, damage, injury, costs or expenses (including reasonable attorney's fees) arising out of or caused by the acts or omissions of Consultant or its employees or agents. Consultant shall also indemnify the NAIC for any taxes, penalties, or other liabilities assessed against Consultant or NAIC under Internal Revenue Code §4980H with respect to any individual Consultant placed at NAIC due to Consultant's failure to (i) offer "minimum essential coverage" under an "eligible employer-sponsored plan" each within the mean of Code §5000A(f)(1)(B); or (ii) offer coverage that is not "affordable" or fails to provide "minimum value" within the meaning of Code §36B(c)(2)(C) and related regulations.

15. RETURN OF PROPERTY

Upon the termination of this Agreement for any reason whatsoever, the Consultant agrees to end all further use and utilization of, and to immediately return to the NAIC, in good condition, all property of the NAIC including, without limitation, any property or equipment furnished by the NAIC or created or prepared by the Consultant, either alone or jointly with others, pursuant to this Agreement. Without limiting the generality of the foregoing, all correspondence, reports, records, charts, materials and other similar data pertaining to the business, activities, research and development, confidential information or intellectual property of the NAIC that are collected by Consultant,

including any and all copies or reproductions thereof, as well as any computer equipment, passwords, access cards, and RSA tokens provided to the Consultant by the NAIC shall be delivered promptly to the NAIC upon termination of this Agreement. In the event that any such items are not so returned, the NAIC will have the right to (a) charge the Consultant for all reasonable damages, costs, attorneys' fees and other expenses incurred in recovering such property, and (b) offset any such expenses against any amount otherwise payable by the NAIC to the Consultant under this Agreement or otherwise.

16. ARBITRATION

Except for claims relating to copyright, trademark issues, trade secrets and confidentiality, any controversy or claim arising out of or relating to this Agreement or the breach thereof shall be settled by arbitration to be held in Kansas City, Jackson County, Missouri, in accordance with the Commercial Arbitration Rules of the American Arbitration Association, and judgment upon the award rendered by the Arbitrator may be entered in any Court having jurisdiction thereof. All arbitration proceedings shall be conducted in the English language. Notwithstanding the foregoing, either party will have the right to seek relief in any court of competent jurisdiction to prevent or enjoin the misappropriation, misuse, infringement or unauthorized disclosure of its confidential information or intellectual property. Both Parties agree not to institute any litigation or proceeding arising from or relating to this Agreement against the other Party except as provided herein.

17. GOVERNING LAW/FORUM/VENUE

By adoption of the Parties, the State of Missouri, U.S.A. is deemed to be the place of contracting and by agreement of the Parties, any claim or controversy relating to this Agreement, its interpretation, performance or validity shall be construed and governed in accordance with the laws of the State of Missouri, without regard to its rules for choice of laws. The Parties herein agree the forum and venue for bringing court action as provided for in this Agreement shall be in Kansas City, Jackson County, Missouri.

18. DATA ACCESS/CYBER HYGIENCE

Dependent on data sources identified, the NAIC will retain responsibility for data and data access as well as appropriate cyber hygiene principals for data storage and administration.

19. MISCELLANEOUS

This Agreement supersedes all other agreements or representations either oral or written between the NAIC and Consultant. No waiver, alteration amendments or modification of provisions in this Agreement shall be binding unless subsequently made in writing and signed by duly authorized representatives of the NAIC and Consultant and appended hereto. If any provision or portion of this Agreement is deemed unenforceable or illegal by operation of law or otherwise, the remaining provisions in the Agreement shall remain enforceable and binding on the parties herein. Consultant's rights and obligations under this Agreement

are not assignable. In the event that any signature is delivered via facsimile transmission or by e-mail delivery of a ".pdf" format file, such signature shall create a valid and binding obligation of the party executing (or on whose behalf such signature is executed) with the same force and effect as if such facsimile or ".pdf" signature page were an original.. The terms of provisions 9, 11, 12, 14, 15, 16, 17, 18 and 19 shall survive termination of this Agreement.



Do you agree to the NAIC Terms & Conditions? Please sign one.

YES	_____Signature	_____Date
NO	_____Signature	_____Date
If NO,	Please provide your Terms and Conditions of Services if you do not agree to the NAIC Terms & Conditions attached.	





October 14, 2024

Commissioner Nathan Houdek, Chair
Financial Condition (E) Committee
National Association of Insurance Commissioners
Via email ddaveline@naic.org

Re: Request for Comments on the Draft Request for Proposal

Submitted Electronically

Dear Mr. Houdek:

The American Council of Life Insurers (ACLI) appreciates the opportunity to comment on the E Committee's August 2, 2024, request for comments on the draft Request for Proposal (RFP) for Credit Rating Providers (CRP) and we support the work that you and your fellow members and staff have put into this project to date.

The ACLI supports the Framework for Regulation of Insurer Investments (the Framework) and recognizes that the NAIC requires further insight into CRP processes to strive to achieve the Framework's goals and initiatives. The draft RFP will serve as the foundation for developing CRP due diligence and should align with the Framework and its directives. There are several areas where the NAIC could enhance this alignment.

General Comments

One goal of the Framework is to provide holistic due diligence around CRP usage, rather than replacing the independent judgment of a CRP. Therefore, the RFP should emphasize that the primary focus of the due diligence review is on CRP processes. This ensures that governance at rating providers is robust, consistent, and effectively addresses conflicts arising from CRPs' commercial incentives, thereby avoiding extreme dispersions. The RFP should facilitate the evaluation and analysis of rating agencies, rather than encouraging a uniformity of thought among them.

Common Expectations

Quantitative analysis and the study of outcomes should be integral to the diligence framework. However, the RFP must emphasize that this due diligence review should allow the ratings market to operate without unnecessary interference. The NAIC's vendor should prioritize avoiding extreme dispersions and outliers in ratings, rather than "herding" CRPs toward a specific result. Any

American Council of Life Insurers | 101 Constitution Ave, NW, Suite 700 | Washington, DC 20001-2133

regulatory herding would undermine the independent judgment of CRPs and risk the NAIC becoming a super rating agency, which it should avoid for legal, reputational, and practical reasons. Such an outcome would stifle the specialization and innovation provided by multiple CRPs in the market, which the Framework seeks to preserve, and could create adverse credit results.

For this reason, we recommend that one focus of the RFP includes a question around the vendor identifying, reviewing, and analyzing rating agencies' asset classes of expertise. Certain asset classes are rated by certain agencies more frequently than others (or to the exclusion of others) due to differences in resources and expertise. Also, because there is significant investment required to create methodologies to review and assess newer and/or more complex asset classes. Not all rating agencies rate every asset class. Any due diligence framework should recognize this specialization and its potential to explain (i) why there is a limited number of rating agencies that provide credit ratings on a given asset class and (ii) what might otherwise be considered a "material dispersion."

The due diligence framework should incorporate transparent data analytics to ensure market confidence in its effectiveness and fairness. Clearly identifying these goals in the RFP will ensure that the vendor's proposed approach addresses them, and that the vendor demonstrates competence in achieving these objectives.

The RFP should also require the vendor to explain how its quantitative and qualitative assessments will address the challenge of level-setting risk across asset classes, given that different risk factors affect various credit segments. Specifically, the RFP should clarify that there are two key quantitative comparisons:

1. **Consistency Across Asset Classes:** How a CRP ensures relative consistency across asset classes (e.g., CLOs vs. Corporates at the same rating point, such as 'A-').
2. **Cross-Agency Ratings:** Ratings for the same asset or asset class across different CRPs (e.g., comparing a CLO rated by S&P (e.g., BBB+) and Moody's (e.g., A-)).

The diligence framework should enhance the NAIC's understanding of the process for level-setting these risks but should refrain from interfering in the market unless there are extreme dispersions.

Additional minimum expectations the RFP should consider include the quality and credibility of asset reviews, the operating structure of the rating agency analysts or teams (e.g., How many deal ratings per analyst? How many people participate in the ratings review/approval process and what are their backgrounds and years of experience?), specific expertise within the agency, and how and when each rating agency issues solicited versus unsolicited ratings. As previously noted, not all rating agencies possess the skills and resources to rate all types of securities. This information will help regulators assess the appropriate SVO resources and understand the limitations of their capabilities.

NAIC Oversight

The draft RFP acknowledges the need for governance and oversight while anticipating input and discussions on these topics. The RFP goals should emphasize the regulators' ultimate authority and role in oversight and final decision-making, ensuring that the diligence framework is built on these foundational assumptions.

With the NAIC's designation now focused on investment risk, vendors will require clear guidance on whether they are assessing investment risk or credit risk in the rating agency due diligence framework. If the focus is on investment risk, we recommend that the NAIC clearly delineates the differences between the two. This presents a valuable opportunity for the SVO to analyze its own resources and processes, enabling the SVO/SSG to benchmark against the CRPs. We suggest involving a regulator who can bridge the gap between credit risk and investment risk, provide insights into how both can be quantified and qualified to ensure consistency in the evaluations of the RFPs.

Thank you for the opportunity to provide feedback on the proposed Request for Proposal. The ACLI is committed to collaborating with the NAIC and state regulators to enhance the RFP process and welcomes further discussion.

Sincerely,

A handwritten signature in cursive script that reads "Shannon Jones".

Shannon Jones
Senior Director - Financial Reporting Policy
Shannonjones@acli.com
202-624-2029



Christopher Anderson, CFA
Principal
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chris@andersoninsights.com

October 1, 2024

Financial Condition (E) Committee
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Comments on the Draft Request for Proposal, August 2, 2024

Dear Commissioner Houdek and Task Force Members,

I appreciate the invitation to respond to the latest draft following up on my comments of March 17th and letter of April 8th. It is evident that the Committee has given a considerable amount of thought concerning how the risks of insurer investments can be assessed in support of NAIC members and this is a very welcome development.

The Committee has already made significant changes to reduce “blind reliance” on CRP ratings through the actions of the SAPWG and the VOS/TF and these will be effective within less than 90 days. Their completion and implementation have somewhat changed the landscape since this past spring and these comments reflect that reality.

The Focus of the RFP

The overall objective of this effort, however, is to answer this question: **“What is the most effective use of regulatory resources in the modern environment of insurer regulation for investments?”** Whether and how to use CRPs is significant but there is more to answering this essential question than deciding the role of the CRPs. This mission will not be completed, then, without further work focusing on how the NAIC, with its limited or even existing or expanded resources, can decide on their “most effective use”.

NAIC Designations Are Now Not the Same As CRP Credit Ratings

It is now established that NAIC Designations reflecting “investment risk” are not necessarily the same as the assessments of “credit risk” by the credit rating providers. It would seem, then, that for the NAIC there needs to be two distinct areas of focus:

- The accuracy and reliability of the credit risk opinions of the CRPs and
- The resources required to translate credit risk opinions into measures of investment risk

Accuracy of Credit Ratings

Of the two, the former should be relatively easy to assess. Comparing projections (credit ratings) to reality (payments as promised vs. defaults) by the CRPs is the true measure of their accuracy. As discussed previously there is a wealth of data available which, when mined effectively, should be not only revealing but can also provide the basis and justification for sound policy decisions.

The many years of the SEC-mandated publicly available Credit Ratings Performance Measurement Statistics for each CRP may only be a starting point. The NAIC itself may very well be the world's largest "consumer" of credit ratings because for years it has received electronic feeds of ratings from all of the CRPs it recognizes. This trove of data could be compared by CUSIP number to the characteristics of public securities making it possible to see performance on an extremely granular level, cutting the data in virtually any way the NAIC may find interesting or useful. Less granular, but still useful, data is also available for the relatively small number of private placements. These are just two examples of available resources.

The consultant charged with assessing the accuracy of CRP ratings has a relatively straightforward technical task primarily involving data manipulation. This requires skills which are not uncommon and it is quite different from other aspects of this engagement. Successful completion could easily result in the development of very specific methods by which the NAIC's information technology staff could assume the responsibility for continuing these analyses well into the future.

Translating Credit Risk Ratings into Investment Risk Measures

This is the hard part. This will require that a consultant possess very specific skills concerning complex investments and knowledge of the NAIC members and their requirements. In the explanation of the difference between credit risk and investment risk (page 10 of this draft) the single example cited is that of principal protected securities. PPSs are, in fact, hybrid securities with some elements of debt along with other elements (typically equity) so they are not pure debt. SAPWG's Principle-Based Bond Definition project and the IAO's purposes and procedures manual have already dealt with PPSs -- they are excluded from bond treatment and relegated to Schedule BA. This addresses one problem.

But while it solves a problem it simultaneously creates quite another one which is very relevant to what a consultant would need to deal with in this engagement. It seems to be intentional that large numbers of assets deemed not to qualify as bonds under the PBBD should not necessarily be assigned an arbitrary and often punitive "standard" BA factor.

This raises the question of how such a factor could be derived and administered. It may be logical to think that the IAO should derive these risk factors but it lacks published methodologies to do so. Furthermore, if assets are not deemed to be eligible for reporting as bonds on Schedule D Part 1 shouldn't the Capital Adequacy Task Force be at least "blessing" the staff methodologies or even developing the risk factor standards itself rather than entrusting this to NAIC staff?

Further Lines of Inquiry

The present system, relying on CRPs and having the IAO fill in gaps, and now review some ratings, has evolved over time. This evolutionary result may actually be found to be ideal, but this is the perfect time to open inquiry, asking if there may be better ways to accomplish the objectives of regulators. My April letter discussed the need for an independent assessment of the capabilities of staff. This is not simply a matter of good governance but it is also directly related to the chances of success of this initiative. Getting a clear understanding of staff capabilities and performance will form the cornerstone for the foundation of expanded responsibilities if that is to be the case. To my knowledge this has not been done in many years so the time is right.

A Broader Inquiry Is Needed To Answer the Question

To truly address the fundamental question of the most effective use, the consultant must be charged with more than making recommendations for how to use CRP ratings. More interesting and complex is how risks will be measured when CRP ratings are not recognized. This needs to be done within the context of a thorough understanding of staff capabilities and performance in order to determine the resources that will

be required in the future. Without this it will be very difficult for a consultant to propose structures that will be workable. The NAIC clearly has no intention of attempting to replicate the work of the 5000+ CRP analysts and supervisors so the consultant will need to assess and evaluate present capabilities in order to propose reasonable enhancements. It is important for the Committee to understand what alternatives to the present system it should consider.

With a solid knowledge of staff capabilities the consultant will then have to tackle these very difficult tasks to fulfil the objectives of the RFP as written:

- How to propose to translate CRP credit ratings into NAIC Designations for literally hundreds of thousands of bonds and
- How to propose to determine when and how to apply investment risk standards when credit measures by themselves are insufficient and -- possibly,
- How to propose to determine risk factors for assets relocated from the bond schedule to Schedule BA

Accomplishing these tasks would be a good beginning.

Should the Scope of the Proposed Engagement be Broadened?

Assessing how well a CRP measures credit risk may turn out to be a relatively straightforward and replicable task. Not so with recommending how the NAIC can develop its own unique measure of what it calls investment risk. Even more challenging, however, would be to fundamentally assess how the NAIC goes about assessing investment risk. This may seem daunting but the benefits of assessing the system overall, not simply assuming that what does exist should exist, could produce great benefits to regulators. The RFP as drafted should provide sufficient information to enable the Committee to evaluate the abilities of respondents to assess the use of CRP ratings but there is potential for much more to be accomplished by expanding its scope.

Respectfully submitted,



Copy: Dan Daveline

Amnon Levy
Bridgeway Analytics
Amnon.Levy@BridgewayAnalytics.com

October 14, 2024

Financial Condition (E) Committee
National Association of Insurance Commissioners
110 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Subject: Comments on the Draft Request for Proposal Regarding the Development of a Due Diligence Program for the Prudent Use of CRPs

Dear Commissioner Houdek and Members of the Financial Condition (E) Committee,

On behalf of Bridgeway Analytics, I appreciate the opportunity to provide comments on the [draft Request for Proposal \(RFP\) aimed at developing a due diligence program for the ongoing use of CRPs](#). We commend the Committee's continued efforts to modernize investment risk oversight, particularly regarding the effective reliance on NAIC credit rating providers (CRPs) through establishing a robust governance structure for due diligence and the evolving role of Securities Valuation Office (SVO) resources.

We strongly support the initiative to reduce the passive (i.e., "blind") reliance on agency ratings while utilizing their output within a robust and transparent due diligence framework. Bridgeway Analytics has previously pointed out that U.S. insurers' investment oversight is somewhat unique compared to other jurisdictions. European bank and insurance guidelines, for example, generally discourage using agency ratings and instead encourage internal models that monitor investment risk when assessing creditworthiness and determining capital requirements.¹ The cost of maintaining these frameworks is significant. For context, the annual cost of running stress tests can exceed \$100 million at some banks, with investment risk monitoring, generally using internal ratings, consuming a significant portion of the cost.² Instead, prudent use of agency ratings, carefully balancing enhanced oversight and associated costs, can provide significant savings for insurers, and the NAIC/regulators, who would otherwise need to assess insurers' internal models, can provide valuable downstream savings to policyholders.

Our letter focuses on CRP Due Diligence and Objectives, the first of three points on which the posted draft RFP requests feedback, particularly its second and third sub-points: (2) Are there additional objectives we should consider that are not included here? (3) Are there objectives that interested parties feel should be excluded, and why? As our letter explains, we encourage the E-Committee to consider a targeted and smaller-scoped, but still significant, proof of concept (POC) exploring the degree to which comparisons of agency rating to corresponding NAIC Designation mappings (i.e., the relative prudence of agency ratings) and SVO's own Designations can be quantitatively measured. In our view, assessing the dimensions and degree to which differences across agencies can be quantitatively measured is needed to guide the more significant effort of

¹ While those jurisdictions offer standardized options, often used by smaller institutions, that can rely on agency ratings for determining capital charges, they generally promote a broader risk assessment approach.

² See, for example, KPMG's [Stress Testing: A benchmark analysis of systemically important financial institutions](#).

designing and implementing the oversight framework. This step will ensure that the design of a robust governance structure for due diligence is built on a robust quantitative foundation.

Our suggestion to begin with a POC is based on our review of methodologies employed by CRPs, the available data, and prior studies that have attempted to quantify the relative prudence of ratings across agencies, which we summarize below. While some studies have demonstrated relative prudence historically in specific markets, to our knowledge, no existing studies have demonstrated significant systematic differences in the prudence of U.S. agency ratings, which is the issue of relevance to regulators.³ To overcome the challenges, our letter proposes a novel approach requiring collecting a consistent set of data from CRPs, which we outline below and in supporting documents. While we believe this innovative approach is both theoretically well-grounded and practical, a targeted POC will demonstrate its value and guide its appropriate use within the broader investment oversight framework.

Rather than a Phase 1 that includes recommendations and considerations on accomplishing the objectives described in the current RFP, consider a smaller-scoped RFP:

- **Targeted POC.** The RFP scope should be a smaller-scoped but still significant POC exploring the degree to which comparisons of agency ratings to corresponding NAIC Designation mappings and SVO's own Designations can be quantitatively measured, along with guidance on how those measures can be used in oversight.
 - **Collect a consistent set of data, initially focusing on public and private corporate credit.** The RFP should request a response to the following questions:
 - Which data should be collected to differentiate prudence across agency ratings and SVO Designations? If details regarding the data are contingent on iterative input from rating agencies and the SVO, please provide context.
 - How will that data overcome known challenges with reliance on historical ratings, which may be based on old methodologies and unavailable for new asset classes?
 - How will that data overcome the known challenges of comparing relative prudence when, for example, debt has few agencies assign a rating or when a single agency rates the security?
 - While Bridgeway Analytics has a view on data that can differentiate relative prudence, we suggest the RFP not narrow the options at this point, allowing RFP respondents to propose alternative approaches. We propose structuring synthetic benchmark portfolios for CRPs to rate and the SVO to assign Designations. The portfolios will consist of synthetic corporate counterparties with a range of balance sheets and financial statements (e.g., leverage ratios, net income, etc.). This new data set will provide a controlled sample of ratings and Designations, facilitating an assessment of the relative prudence of CRPs and the SVO using their current methods.
 - **An analysis of relative CRP rating and SVO Designation prudence measures.** The deliverables should include an assessment of the dimensions and degree to which CRP ratings and SVO Designation differences can be quantitatively measured.
 - **Provide guidance on using relative prudence measures in designing and implementing the oversight framework.** The deliverables should include assessing how the measures can guide the more significant effort of designing and implementing the oversight framework, ensuring the governance structure for due diligence is built on a robust quantitative foundation. The RFP should explain that the more significant effort of designing and implementing the oversight framework would be a subsequent Phase; that effort would look much more like the current DRAFT RFP.

³ See, [Race to the Bottom? Competition Among Rating Agencies in the European Structured Debt Market – Evidence from the CRA Regulation](#).

- **Aspirational features.** The RFP should include the need for the data and guidance to have these additional features, which will ensure the ultimate framework is robust:
 - A mechanism incenting CRPs to provide the necessary information, acknowledging they have no commercial interests to support the effort in earnest. In addition, the RFP should provide guardrails on requirements that can be placed on CRPs that are sensitive to limits to insurance regulators' jurisdictional mandates.
 - The need for market oversight, with transparency and incentives for market participants (e.g., insurers and their asset managers) to flag data that might lead to misleading conclusions over relative prudence (e.g., ratings on synthetic benchmark portfolios that do not conform with an agency's true standards). For example, if the NAIC and state regulators are the only consumers of the analysis, the framework will lack a natural market oversight mechanism.
 - Emphasize approaches that can evolve naturally with capital markets, with sensitivity to confidential information.

Our letter explores the following issues in detail:

- Placing Additional Reporting Requirements on CRPs
- Current Data Limitations: The Need to Collect Consistent Data
- Data Complexities and Required Efforts by CRPs
- The Need for Market Oversight and an Evolving Process

Our letter concludes with a summary of our suggested refinements to the RFP and the next steps for the E-Committee to consider.

1 Placing Additional Reporting Requirements on CRPs

The draft RFP poses an important question of which safeguards should be implemented to ensure that the NAIC does not violate the Credit Rating Agency Reform Act.

The question aligns with comments at the E-Committee meeting on August 29, 2024, that led to adopting a process for extending NAIC staff discretion over CRP rating-based Designations. The comments served as a reminder that while the U.S. Securities and Exchange Commission (SEC) oversees rating agencies, state insurance regulators are consumers of ratings. Neither the NAIC nor insurance regulators have the authority to regulate rating agencies. In that regard, the discretion process was laid out in a manner that is sensitive to jurisdictional guardrails and does not require the rating agency to be involved in the review process, although they have the option to join if invited by an affected insurer.

Meanwhile, the draft RFP requests specific data fields from CRP applicants (i.e., under Sources of Data). The NAIC is not new to placing disclosure requirements on CRPs beyond those required by the SEC for Nationally Recognized Statistical Rating Organizations (NRSROs). Rating rationale reports are currently required for private ratings to be used in the Designation process in the form of a private letter rating (i.e., PLR).

It would be helpful if the RFP provided guidance on the degree to which heightened disclosure requirements on NRSROs to qualify as CRPs are appropriate, which we explore further in subsequent sections.

2 Current Data Limitations: The Need to Collect Consistent Data

Variation in approaches limits the comparability of relative prudence across CRP methodologies. CRPs employ varied methods and standards across asset classes, with elements that can be subjective and inputs that can be

proprietary. This greatly limits the degree to which ratings can be replicated or the degree to which it is possible to make informed inferences of relative prudence based on an assessment of methodologies. This is particularly relevant with structured assets, where the risk profiles are inherently complex and require nuanced analysis.

Data limitations limit the comparability of relative prudence across agencies. Measuring default risk, which is inherently remote, is challenged by the dearth of credit events requiring long historical samples coupled with methods employed by CRPs changing over time. The degree to which it is possible to make informed inferences of relative prudence based on past ratings, especially for new asset classes and rating methodologies, is extremely challenging, except for a handful of market segments.

The NAIC is not alone in its efforts to overcome challenges with level-setting ratings and CRP performance. In Europe, the relevant authorities map agency ratings and their Credit Quality Step scale. They do this predominantly by studying historical default data subject to their own [Technical Standards](#). While this process may result in a mapping where some agencies are notched relative to others, no notching is being applied under the current mapping, and we are aware of only two cases historically where notching occurred.

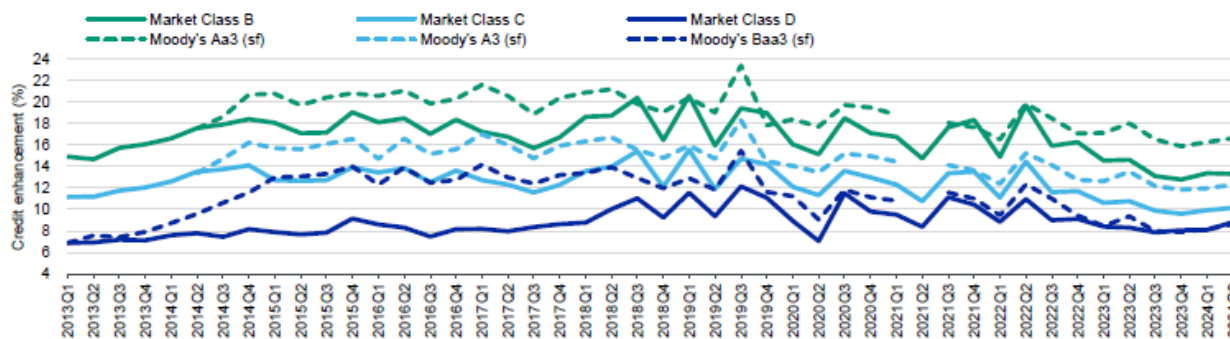
Some studies have demonstrated relative prudence historically in specific markets. For example, European guidelines require rated securitizations to have at least two agency ratings, allowing for a cross-sectional comparison of public ratings across agencies that rate transactions.⁴ However, the data would not allow for the analysis of private ratings, CRPs that rate few transactions, or new or evolving asset classes. Regardless, in the U.S., there are no guidelines requiring two agency ratings, and the set of securities with multiple agency ratings is much smaller, making comparisons significantly less viable. For example, [Benchmarking the Treatment of CLOs](#) compares CMBS tranche S&P and Moody's ratings. That analysis, taken in isolation, suggests that S&P and Moody's relative prudence is comparable since the historical ratings are highly correlated, but the relevance of this finding is unclear for privately rated debt and debt rated by a single agency.

Exhibit 8 of Moody's report, CMBS, and CRE CLOs – U.S. Sector Update – Q3 2024 (reproduced below) tells a very different story. Credit enhancement for CMBS conduit deals in which Moody's rates at least one bond class are analyzed. Moody's generally requires significantly higher CE levels on the Market Class B (C or D), which receives an Aa3(sf) (A3(sf) or Baa3(sf)) or equivalent in the market. The exhibit suggests that bonds with a market-equivalent Aa3(sf) rating would receive a Moody's A3(sf) rating over certain periods, for example.

⁴ See, [Dealing with the conflicts of interest of credit rating agencies: a balanced cure for the disease](#).

Exhibit 8

Average junior IG tranche credit enhancement for conduit deals in which we rate at least one bond class



Class B tranches receive a minimum rating of Aa3 (sf) or equivalent in the market; Class C receives A3 (sf) or equivalent; Class D receives Baa3 (sf) or equivalent. We rated only one conduit transaction in Q2 2021, so our indicative CE for the junior classes is omitted for the quarter.
Sources: Trepp, LLC and Moody's Ratings

Punchline. The nature of the ratings process often incentivizes investors to have agencies report only more favorable ratings, resulting in censored observations and a lack of comparability if only historical data are used. [Overseeing Designations and the Prudent Use of Agency Ratings](#) explores this issue at great length and proposes a synthetic benchmark portfolio approach to overcome these challenges.⁵ The approach has each CRP rate the same set of synthetic benchmark credit portfolios, allowing an assessment of their relative prudence. This new data set will provide a controlled sample of ratings and Designations, facilitating an assessment of the relative prudence of CRPs and the SVO using their current methods. This avoids the challenge of relying on historical ratings, which may be based on old methodologies. The approach overcomes the challenge of comparing relative prudence when, for example, debt has few agencies or when a single agency rates the security.

If this path is taken, we suggest first focusing on public and private corporate ratings since the methodologies and data CRPs employ are better understood than other asset classes; if the approach does not provide insights for corporate credit, it is unlikely to provide insights for the broader set of asset classes. If privately rated corporate credit is included, the study would systematically analyze the relative prudence of CRP ratings for an asset class flagged as concerning. This approach has the benefit of increasing the likelihood of the POC providing value to the NAIC and state regulators regardless of the conclusions reached regarding the viability of the broader effort.

3 Required Efforts by CRPs

The variation in data that describes the risks across different asset classes is significant (e.g., corporate, municipal, real estate, and asset-backed securities). Even within the class of corporate credit, CRPs often rely on a range of financial statement data along with adjustments to reflect security-specific features (e.g., notching for subordinated debt). Rating the same sets of benchmark portfolios requires an effort that agencies would otherwise not take on. The E-Committee should consider mechanisms to ensure CRPs are incented to support the effort in earnest. Unless required, an agency has no commercial incentive to substantively support developing the process and rate the benchmarks. One mechanism worth considering requires CRPs to provide the necessary asset class-specific data as part of the qualifying CRP process, allowing their ratings to be used in the Designation process. Of course, this comes back to the question above regarding the degree to which there is an appetite to place additional reporting requirements on CRPs.

⁵ Also see [Investment Risk Oversight](#).

4 The Need for Market Oversight and an Evolving Process

We have previously pointed to the benefits of market oversight on public ratings, whereby market participants flag ratings that do not conform with expectations. In a similar spirit, we encourage the E-Committee to consider including a requirement in the RFP that the due diligence process for overseeing CRP ratings should aspire to incorporate a similar market mechanism. The process should be transparent and incent market participants (e.g., insurers and their asset managers) to flag data that might lead to misleading conclusions over relative prudence (e.g., ratings on synthetic benchmark portfolios that do not conform with an agency's true standards).

Similar to concerns with private ratings lacking market oversight, we encourage the E-Committee to be sensitive to the resulting lack of oversight if the NAIC and state regulators are the only consumers of the analysis. In the context of having insurers use CRP ratings in business applications beyond regulatory requirements, including their use in Designations, to demonstrate their credibility, measures intended to address regulatory requirements narrowly can lack credibility.

Finally, we encourage emphasizing approaches that can evolve naturally with capital markets, with sensitivity to confidential information.

5 A Measurement POC for the RFP Scope and the Next Steps

Rather than a Phase 1 that includes recommendations and considerations on accomplishing the objectives as described in the current RFP, we suggest the E-Committee consider a smaller-scoped RFP:

- **Targeted POC.** The RFP scope should be a smaller-scoped but still significant POC exploring the degree to which comparisons of agency ratings to corresponding NAIC Designation mappings and SVO's own Designations can be quantitatively measured, along with guidance on how those measures can be used in oversight.
 - **Collect a consistent set of data, initially focusing on public and private corporate credit.** The RFP should request a response to the following questions:
 - Which data should be collected to differentiate prudence across agency ratings and SVO Designations? If details regarding the data are contingent on iterative input from rating agencies and the SVO, please provide context.
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 - While Bridgeway Analytics has a view on data that can differentiate relative prudence, we suggest the RFP not narrow the options at this point, allowing RFP respondents to propose alternative approaches. We propose structuring synthetic benchmark portfolios for CRPs to rate and the SVO to assign Designations. The portfolios will consist of synthetic corporate counterparties with a range of balance sheets and financial statements (e.g., leverage ratios, net income, etc.). This new data set will provide a controlled sample of ratings and Designations, facilitating an assessment of the relative prudence of CRPs and the SVO using their current methods.
 - **An analysis of relative CRP rating and SVO Designation prudence measures.** The deliverables should include an assessment of the dimensions and degree to which CRP ratings and SVO Designation differences can be quantitatively measured.
 - **Provide guidance on using relative prudence measures in designing and implementing the oversight framework.** The deliverables should include assessing how the measures can guide the more significant effort of designing and implementing the oversight framework, ensuring the governance

structure for due diligence is built on a robust quantitative foundation. The RFP should explain that the more significant effort of designing and implementing the oversight framework would be a subsequent Phase; that effort would look much more like the current DRAFT RFP.

- **Aspirational features.** The RFP should include the need for the data and guidance to have these additional features, which will ensure the ultimate framework is robust:
 - A mechanism incenting CRPs to provide the necessary information, acknowledging they have no commercial interests to support the effort in earnest. In addition, the RFP should provide guardrails on requirements that can be placed on CRPs that are sensitive to limits to insurance regulators' jurisdictional mandates.
 - The need for market oversight, with transparency and incentives for market participants (e.g., insurers and their asset managers) to flag data that might lead to misleading conclusions over relative prudence (e.g., ratings on synthetic benchmark portfolios that do not conform with an agency's true standards). For example, if the NAIC and state regulators are the only consumers of the analysis, the framework will lack a natural market oversight mechanism.
 - Emphasize approaches that can evolve naturally with capital markets, with sensitivity to confidential information.

Beyond our suggested refinements to the RFP, we encourage the E-Committee to consider interim steps to support investment risk oversight (beyond CRP rating oversight). Acknowledging the timelines for developing an approach in the spirit of the one outlined in the draft RFP, we encourage the E-Committee to consider additional governance mechanisms that can be rolled out more quickly, which we discuss in our reports [Overseeing Designations and the Prudent Use of Agency Ratings](#) and [Investment Risk Oversight](#), that include:

- **Supervisory standards.** Introducing investment risk oversight standards, including model risk management standards similar to those laid out in [Supervisory Guidance on Model Risk Management](#) (SR 11-7), which the U.S. Board of Governors of the Federal Reserve System Office of the Comptroller of the Currency put forth, or [Actuarial Standard of Practice No. 56, Modeling \(ASOP No. 56\)](#).
- **Credible use of CRP ratings.** Requiring insurers to demonstrate their use of CRP ratings in business applications beyond regulatory compliance could provide transparency without necessitating the development of entirely new systems or frameworks. This demonstration can be assessed and incorporated into insurers' Risk-Focused Surveillance Cycle and Financial Examinations. This approach aligns with Principle 6 of the Investment Framework Workplan, which asserts that insurers themselves bear the ultimate responsibility for prudent investment oversight.
- **Modernizing other elements of investment risk oversight, including RBC.** Modernizing other elements of the investment risk oversight process in its aspirations of *equal capital for equal risk, with consideration of tail risk*. While several initiatives to level-set capital across asset segments and their risks are underway, including differentiating the treatment of collateralized loan obligations and other targeted items, a holistic revamp of the RBC framework for investments has not been discussed, to date. Developing a capital framework, in many regards, requires fewer resources than a quantitative process for ongoing oversight of Designations. Designations are assigned to each of the ~250,000 individual securities held and require ongoing monitoring. On the other hand, capital frameworks are not updated frequently and are coarse, with only 20 C-1 (R-1) bond factors for those ~250,000 securities.

We are optimistic that the NAIC's efforts, supported by a well-considered RFP, will lead to a more robust and resilient investment risk oversight framework. Bridgeway Analytics is committed to supporting these initiatives and looks forward to continued engagement with the E-Committee and the NAIC.

Thank you for considering our views on this critical issue. We welcome further discussions or clarifications as the E-Committee progresses with this important work.

Sincerely,

A handwritten signature in black ink, appearing to read 'Amnon Levy', written over a horizontal line.

Amnon Levy
Founder and Chief Executive Officer

Bridgeway Analytics supports the investment and regulatory community work to optimize the design, organization, and utility of regulations surrounding the management of insurance company portfolios. While the content in this document is informed by extensive discussions with our client base, the broader industry, NAIC staff, and state regulators and may contain analysis that Bridgeway Analytics had conducted as part of a commercial engagement and retains the right to reuse, the views in this document are solely those of Bridgeway Analytics and are based on an objective assessment of data, modeling approaches, and referenced documentation, that in our judgment and experience, are viewed as appropriate in articulating the issues at hand. Methodologies are available to the public through an email request at support@bridgewayanalytics.com. For more information, visit www.BridgewayAnalytics.com.



Commissioner Nathan Houdek
 Financial Condition (E) Committee
 National Association of Insurance Commissioners
 Via Email: Dan Daveline, ddaveline@naic.org

RE: Request for Comments on the Draft Request for Proposal

Dear Commissioner Houdek,

Thank you for the opportunity to comment on the Draft Request for Proposal (“Draft”). The National Association of Mutual Insurance Companies and the American Property and Casualty Insurance Association (the “Trades”) understand the goal of the National Association of Insurance Commissioners (“NAIC”) with the Draft and is appreciative of the noted legitimate and significant challenges that lay ahead with modernizing the role of the Securities Valuation Office (“SVO”) to better analyze companies and their solvency. The answer to the question “what is the most effective use of regulatory resources in the modern environment of insurance regulation for investments” is nuanced and may differ from state to state. The Trades offers the following comments for consideration, organized according to the exposed Draft.

CRP Due Diligence and Objectives

- (1) Are all objectives clear and understood? Do any need to be refined?

“Quantitative Analysis” references the NAIC’s ability to utilize data to validate a credit rating provider’s (“CRP”) mapping of its NRSRO rating to corresponding NAIC designation or create a NAIC mapping. Are there any administrative barriers that prevent the NAIC from being able to develop this currently?

“Sources of Data” asks the applicant to utilize existing data that the NAIC has or receives. This clear and concise definition is appreciated. However, if other data sets are needed, the consultant and NAIC staff should work with industry to understand what data “is most easily obtained.” This process should not lead to the collection of data that is difficult for companies to organize, format, and produce.

“Ongoing Review” references an examination process that state regulators can utilize to provide oversight of the SVO in its implementation of this frameworks, its own production of designations and its usage of individualized challenges to CRP ratings in the designation process. The E Committee just recently adopted changes to the CRP filing exempt process. Is the NAIC



envisioning something different than was just adopted? Would this proposed state regulator examination process be subject to exposure and adoption at the Committee level?

- (2) Are there additional objectives we should consider that are not included here?

Under “*Other Considerations for CRP Qualifications*”, the Trades ask that the Committee consider agreed upon regulatory control of data and data access as well as appropriate cyber hygiene principles for data storage and administration, including third party vendors. The third-party vendor selected will have the ability to utilize and see the data that all insurance companies, not just P/C, submit to the SVO. There must be appropriate and clearly stated guardrails around the interaction with the data, such as data collection, notice, storage, and confidentiality requirements. These guardrails should also extend to the due diligence framework and system once it is fully implemented.

- (3) Are there objectives that interested parties feel should be excluded, and why?

No objectives to be excluded.

RFP Response Requirements

- (1) Are all requirements clear and understood? Do any need to be refined?

The requirements are clear and understood.

- (2) What additional response requirements could be included to ensure the best receipt of material selection purposes?

The Trades have no comments on this item.

- (3) Are there response requirements that interested parties feel should be excluded, and why?

The Trades have no comments on this item.

Selection Process and Assessment Criteria

- (1) Is the selection process clear and understood?

The selection process is clear and understood.

Other

- (1) Any other feedback that would aid in improving the RFP.



The Trades are curious how the NAIC envisions this project's staffing needs long-term. Will third-party contractors be performing the work on an on-going basis or until the NAIC is able to hire the appropriate amount of qualified full-time personnel? It is the Trades' belief that if the NAIC chooses to use a third-party contractor, the guardrails mentioned above should apply to ensure data protection and confidentiality.

Thank you for your consideration of these comments on this matter of importance to insurers and policyholders. We look forward to continuing the dialogue on these issues and being helpful to moving these discussions forward.

Colleen W. Scheele
Public Policy Counsel and Director of Financial and Tax Policy
National Association of Mutual Insurance Companies (NAMIC)

Matthew Vece
Director, Financial & Tax Counsel
American Property Casualty Insurance Association (APCIA)

October 14, 2024

Dan Daveline
Director of Financial Regulatory Services
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Request for Comment on the Draft Request for Proposal – Credit Rating Provider Due Diligence Framework

Dear Mr. Daveline:


KBRA appreciates the opportunity to provide feedback on the National Association of Insurance Commissioners' ("NAIC") Draft Request for Proposal – Credit Rating Provider Due Diligence Framework (the "Due Diligence Framework"). As a credit rating provider ("CRP"), KBRA's core mission is to provide independent, transparent, and thorough credit analysis and research. We welcome initiatives that are aligned with these objectives and that are consistent with broader legal, regulatory and policy principles for the oversight of credit rating agencies ("CRAs"). In its current form, the Due Diligence Framework is at odds with these objectives and risks undermining these principles. As discussed in further detail below, our concerns fall into three categories:

- 1. The Due Diligence Framework incorrectly suggests that CRP credit ratings are not subject to meaningful regulatory oversight.** National Recognized Statistical Rating Organizations ("NRSROs"), which pursuant to the Purposes & Procedures Manual of the NAIC Investment Analysis Office are the only rating providers able to provide Credit Rating Services to the NAIC,¹ are subject to the oversight of the U.S. Securities and Exchange Commission ("SEC") in accordance with federal law.² Contrary to indications in the Due Diligence Framework, the SEC provides robust oversight of the practices of NRSROs in determining credit ratings while also preserving credit rating agency independence, fostering competition and promoting efficiency in capital markets.
- 2. The Due Diligence Framework should not create market uncertainty by interfering with existing regulatory oversight of CRPs.** The Due Diligence Framework indicates that the NAIC "acts solely as a private consumer of credit ratings" and "disclaims any authority to regulate CRPs or rating organizations," yet the Due Diligence Framework is intended to empower the NAIC to effectively operate as a parallel regulator of the SEC in its oversight of NRSROs.³ It is unclear how the Due Diligence Framework will operate in parallel with the SEC's oversight of NRSROs without

¹ Purposes & Procedures Manual of the NAIC Investment Analysis Office (December 2023) at page 19, *available at* https://content.naic.org/sites/default/files/ppm-oss-2023_0.pdf.

² This includes, among other things, the Dodd–Frank Wall Street Reform and Consumer Protection Act and the Credit Rating Agency Reform Act of 2006 (CRARA), including the regulations promulgated thereunder by the SEC.

³ See e.g., Due Diligence Framework at page 2 ("There are currently no criteria for becoming a CRP beyond being an U.S. Securities and Exchange Commission (SEC) registered NRSRO and under its regulatory authority, the SEC is unable to opine on the quality of NRSRO methodologies and ratings. As such, the NAIC "blindly" relies on the CRP ratings. There is no mechanism for overall due diligence around CRP usage, no process to assess the reasonability of a CRP's ratings, nor an ability to challenge an individual rating for not conforming to regulator expectations of how it was determined. Based on this Framework, the NAIC is planning several workstreams to address the issues identified.").



introducing material inconsistencies, threatening CRP independence, and undermining competition in the broader credit rating agency market.

- 3. The Due Diligence Framework is unlikely to produce meaningful analytical results.** The Due Diligence Framework is unlikely to produce meaningful analytical results because it misconstrues the nature of credit risk analysis amongst CRPs. CRPs apply independent credit rating definitions and methodologies to arrive at independent credit ratings. In order to accurately reflect the nature of credit risk analysis, the Due Diligence Framework would need to consider a significant range of additional factors not currently reflected in the proposal.

In the attached Annex I, we discuss these views in further detail. In the attached Annex II, we provide an overview of existing SEC Requirements for NRSROs. We thank you for your consideration of our comments and look forward to continued engagement with the NAIC on the Due Diligence Framework. KBRA is committed to providing constructive feedback and information to the NAIC as the process continues and remains available to be of further assistance.

Sincerely,

/S/ Kate Kennedy
Senior Managing Director
Co-Head of Business Development

ANNEX I

1. The Due Diligence Framework Incorrectly Suggests That CRP Credit Ratings Are Not Subject to Meaningful Regulatory Oversight

The Due Diligence Framework is intended to close a perceived gap in the existing oversight of NRSROs by the SEC, but the proposal fails to consider the nature and full extent of the regulatory oversight of NRSROs pursuant to federal law and regulation. While we appreciate the NAIC has a vested interest in the quality of credit ratings utilized for insurance regulatory purposes, we suggest the Due Diligence Framework should leverage the existing regulatory framework for NRSROs and its underlying principles.

The primary purpose of the NRSRO regulatory framework is to protect investors and users of credit ratings, including the NAIC.⁴ However, the rationale for the Due Diligence Framework rests on the assertion that the “SEC is unable to opine on the quality of NRSRO methodologies and ratings,” and “as such, the NAIC ‘blindly’ relies on the CRP ratings,”⁵ and therefore, seeks to establish “a robust and effective governance structure for the due diligence of CRPs.”

In fact, CRPs are subject to comprehensive regulatory oversight by the SEC in accordance with the Credit Rating Agency Reform Act (“CRARA”)⁶ and the Dodd-Frank Wall Street and Consumer Protection Act (the “Dodd-Frank Act”).⁷ Through rulemaking, examination and enforcement, the SEC provides oversight of the practices of NRSROs in determining credit ratings for the protection of users of credit ratings and in the public interest; promotes accuracy in credit ratings issued by NRSROs; works to guard against credit ratings issued by NRSROs that are unduly influenced by conflicts of interest; and promotes greater transparency and disclosure to investors by NRSROs.⁸

The regulatory requirements for NRSROs include, but are not limited to, publishing all methodologies used to derive credit ratings, qualifying exams for credit analyst staff, as well as other company controls, processes, and extensive policies around conflicts of interest. Further, the SEC conducts annual examinations which include onsite meetings where examiners query analysts, compliance, and credit policy staff on granular aspects of policies, procedures, and individual transaction ratings analyses. The SEC also requires that NRSROs publicly disclose credit rating performance statistics that include the initial credit ratings and any subsequent changes to those ratings to allow credit rating users to evaluate them for accuracy and compare the performance of ratings across NRSROs.⁹

Additionally, as required by law, the SEC publishes an annual report detailing its findings on its examinations of the NRSROs, and to discuss the state of competition, transparency, and conflicts of interest among them. If the SEC determines that an NRSRO does not adhere to applicable laws and regulations, the SEC is empowered to censure the NRSRO, limit its activities, suspend its registration for

⁴ According to the Due Diligence Framework, “the NAIC acts solely as a private consumer of credit ratings” and “disclaims any authority to regulate CRPs or rating organizations.” Due Diligence Framework, Policy and Legal Disclosure Pertaining to the NAIC Credit Rating Provider (CRP) List at page 9.

⁵ Due Diligence Framework at page 2.

⁶ Credit Rating Agency Reform Act of 2006, Pub. L. No. 109-291, 120 Stat. 1327 (2006).

⁷ See *infra* Annex II for an overview of requirements for NRSROs under SEC rules.

⁸ SEC: About the Office of Credit Ratings, available at <https://www.sec.gov/about/divisions-offices/office-credit-ratings/about-office-credit-ratings>.

⁹ See *infra* Annex II for additional information.

up to 12 months, or revoke its registration.¹⁰ To suggest that the SEC is effectively powerless in its regulatory oversight of NRSROs is erroneous and a mischaracterization of its authority.

The Due Diligence Framework nevertheless suggests that the absence of regulatory oversight of the content of specific credit ratings is a gap which the NAIC must close.¹¹ As the NAIC attests, there is not “an ability to challenge an individual rating for not conforming to regulator expectations of how it was determined,”¹² an issue the NAIC is seeking to rectify under the Due Diligence Framework. However, the CRARA expressly states that “neither the Commission nor any State (or political subdivision thereof) may regulate the substance of credit ratings or the procedures and methodologies by which any nationally recognized statistical rating organization determines credit ratings.”¹³ This restriction against government and regulatory interference in methodological and analytical independence is a cornerstone principle in the oversight of credit rating agencies globally.¹⁴ It serves to preserve the integrity of the credit rating process and instill market confidence that credit ratings accurately reflect the credit rating agency’s analysis in accordance with its published methodologies.

The existing regulatory framework for NRSROs also reflects congressional intent to support and encourage competition in the credit rating agency market. In the wake of the Global Financial Crisis (the “GFC”), the Dodd-Frank Act introduced new measures to both improve the quality of NRSRO credit ratings and support further competition in the credit rating agency market.¹⁵ This competition fosters diversity of opinion among credit rating agencies, provides investors with more options, and reduces the risk that credit rating agencies move in lockstep with one another.

In contrast, the Due Diligence Framework appears designed¹⁶ to further broader NAIC policy objectives to promote uniformity among credit rating agencies.¹⁷ In fact, this drive toward uniformity among CRAs is

¹⁰ Under Section 15E(d) (15 U.S.C. § 78o-7(d)), the SEC is authorized to suspend or revoke the registration of an NRSRO if, after notice and a hearing, the SEC finds that the NRSRO has failed to comply with the applicable regulations or provisions of the law.

¹¹ Due Diligence Framework at pages 1-2.

¹² Due Diligence Framework at page 2.

¹³ Section 15E(c)(2) (15 U.S.C. § 78o-7(c)(2)).

¹⁴ See e.g., Article 23(1) of Regulation (EC) No 1060/2009 of the European Union that specifies that governments cannot interfere with the content of credit ratings or methodologies of credit rating agencies.

¹⁵ For example, by making NRSRO methodologies and rating histories more transparent, it is easier for investors to compare ratings from different agencies and may encourage the use of a broader set of NRSROs. See Section 932 of the Dodd-Frank Act. The Dodd-Frank Act also required reduced regulatory reliance on credit ratings to, among other things, prompt investors to rely less on ratings and perform their own credit risk assessments, potentially fostering demand for ratings from smaller agencies. See Section 939A of the Dodd-Frank Act. Further, the Dodd-Frank Act included a proposal for the SEC to study the feasibility of a rule that would require issuers of securities to periodically rotate the credit rating agencies they use. See Section 939F of the Dodd-Frank Act. This measure considered long-term relationships between issuers and particular rating agencies and how to foster more competition by giving smaller agencies opportunities to enter the market. *Id.*

¹⁶ Due Diligence Framework, pages 15-16.

¹⁷ See e.g. NAIC Capital Markets Bureau Special Report: *Growth in Private Ratings Among U.S. Insurer Bond Investments and Credit Rating Differences*, pg. 6 (May 2024) (“Regulatory Framework Overseeing Rating Agencies Does Not Result in Uniform Ratings - The Credit Rating Agency Reform Act of 2006 (“CRARA”) requires rating agencies seeking NRSRO recognition to make their methodology information publicly available to foster accountability, transparency, and competition among the credit ratings industry. The CRARA aims to make the differences between rating agencies and their methodologies visible to enable users of ratings, like insurance companies and the NAIC, to make informed decisions about the strengths and weaknesses of individual rating agencies’ methodologies and, thereby, their ratings. However, there is currently no regulatory oversight to monitor or assess the uniformity or quality of credit ratings, nor any uniformity among the rating agencies themselves.”). The NAIC focus on uniformity is also reflected in recently approved amendments to the P&P Manual designed to “promote uniformity in the production of NAIC designations.” Paragraph 80, *Revised Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the “P&P Manual”) Authorizing the Procedures for the SVO’s Discretion Over NAIC Designations Assigned Through the Filing Exemption Process*). Similarly, the amendments indicate “the Credit Committee will convene to determine if, in its opinion, the NAIC Designation Category assigned pursuant to the filing exemption process is a reasonable assessment of investment risk of the security for regulatory purposes. As part of its review, the Credit Committee may consider



inconsistent with the SEC's conclusions regarding standardization among CRAs. As required by the Dodd-Frank Act, the SEC conducted a study on the merits and feasibility of standardizing: (i) credit ratings terminology; (ii) market stress conditions under which ratings are evaluated; (iii) quantitative correspondence between credit ratings and range of default probabilities and loss expectations under standardized conditions of economic stress; and (iv) terminology across asset classes, so that named ratings correspond to a standard range of default probabilities and expected losses independent of asset class and issuing entity.¹⁸ Citing the numerous difficulties and concerns identified in its study,¹⁹ the SEC staff recommended that no action should be taken to promote standardization in these areas, and instead, the focus should be on the initiatives under Dodd-Frank designed to promote transparency with respect to the performance of credit ratings and the methodologies used to determine credit ratings.²⁰ The standardization of credit ratings, however, seems to be a key goal for the outcome of the Due Diligence Framework.²¹

The regulatory framework for NRSROs is well-developed, comprehensive, and reflects critically important principles to promote and protect the quality and independence of credit ratings. Rather than developing an entirely separate and redundant due diligence regime that is at odds with these principles, we would encourage the NAIC to leverage the tools and information already available under the existing federal NRSRO regulatory framework to meet its objectives.

2. The Due Diligence Framework Should Not Create Market Uncertainty by Interfering with Existing Regulatory Oversight of CRPs

Even more troubling than potential redundancy with the existing NRSRO framework, the Due Diligence Framework risks interfering with existing regulatory oversight of CRPs by: (i) potentially undermining CRP independence; and (ii) reaching inconsistent outcomes with the SEC's oversight. It is unclear how the Due Diligence Framework will operate in parallel with the SEC's oversight of NRSROs without introducing material inconsistencies, threatening CRP independence, and undermining competition in the broader credit rating agency market.

As discussed, one of the most important features of the NRSRO framework is the prohibition of government interference in the content of credit ratings and credit rating methodologies. This prohibition is critical to guard against actual or perceived government influence on credit ratings. Regardless of the source, any form of outside influence which potentially impacts the analytical independence of CRPs harms investors and undermines the integrity of the broader market. The Due Diligence Framework, however, is designed specifically to assess the quality of credit ratings, as opposed to whether the CRP credit rating process is of sufficient quality.

The Due Diligence Framework also risks introducing inconsistent outcomes with SEC oversight of NRSROs which would in turn introduce broader market uncertainty and inefficiency. For example, under the Due Diligence Framework, the NAIC could determine that an NRSRO CRP or a subset of its credit ratings are of

observable factors including, but not limited to (I) a comparison to peers rated by different CRPs..." Paragraph 166, *Revised Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the "P&P Manual") Authorizing the Procedures for the SVO's Discretion Over NAIC Designations Assigned Through the Filing Exemption Process*.

¹⁸ See SEC Report to Congress: Credit Rating Standardization Study as Required by Section 939(h) of the Dodd-Franke Wall Street Reform and Consumer Protection Act (September 2012) (the "SEC Standardization Study"), available at https://www.sec.gov/files/939h_credit_rating_standardization.pdf.

¹⁹ See Executive Summary of SEC Standardization Study at pages 1-5.

²⁰ *Id.*

²¹ Due Diligence Framework at pages 15-16.



insufficient quality for NAIC purposes. At the same time, the SEC may not have reached a similar conclusion or acted with respect to the credit rating agency's NRSRO status. This inconsistency may cause investors to question the NRSRO framework, the credibility of SEC oversight, as well as the NAIC's due diligence of CRPs. The discrepancy may also lead investors and other market participants to question the quality of the CRP's credit ratings more broadly and whether those credit ratings appropriately reflect credit risk or could be subject to further scrutiny, downgrades, or withdrawal. This would lead to unnecessary confusion among investors and potentially destabilize the markets.

The NAIC recognizes that the Due Diligence Framework poses these risks, including potentially violating federal law, unless safeguards are in place.²² The NAIC can avoid these risks by first leveraging existing SEC oversight of the NRSRO framework rather than seeking to replace, replicate or supersede it through the Due Diligence Framework. This would enable the NAIC to meet its objectives in parallel with the SEC and without violating the CRARA and disrupting markets more broadly.

3. The Due Diligence Framework is Unlikely to Produce Meaningful Analytical Results

The Due Diligence Framework is unlikely to produce meaningful analytical results because it misconstrues the nature of credit analysis amongst CRPs. CRPs apply independent credit rating definitions and methodologies to arrive at independent credit ratings. For example, unlike auditors that attest to the conformity of financial statements to unified principals and standards in Generally Accepted Accounting Principles ("GAAP") and International Financial Reporting Standards ("IFRS"), each agency acts independently to produce ratings for a given asset class which will perform in accordance with its own ratings definitions and methodologies. As noted earlier, there is no government authority or organization that puts forth rules designed to influence the content of credit rating agency methodologies or the content of credit ratings, nor should there be as this would violate federal law. The diversity of opinion and approaches among credit rating agencies serves the capital markets well by providing for a variety of opinions on the credit quality of individual instruments.

In order for the Due Diligence Framework to provide meaningful results from an analytical perspective, each CRP's individual rating definitions must be considered because CRP methodologies are intended to produce results in accordance with the CRP's definitions. Furthermore, the CRP's approach to methodologies can differ such that some methodologies are more principles-based while others can be more rules-based. As a result, the methodology should be compared in tandem with actual credit rating reports, including new issuance and surveillance reports, in order to apply and evaluate the specific methodology.

Similarly, the Due Diligence Framework appears to consider the CRP credit rating in isolation or in absolute terms. Where two CRPs rate a given instrument, we would recommend that more than just the rating level should be considered; the quality of the related rating report, methodology, and rating stability need to be factored into the assessment.

We also note that any evaluation of credit ratings should consider bias, from the perspective of CRP selection, as well as the potential for incumbent CRPs to have a greater share of larger credits relative to newer entrants. In order to enter the highly concentrated credit rating agency market, newer CRPs may rate a disproportionate number of less capitalized entities relative to their incumbent CRP peers that historically rate more of the larger credits. The larger credits may be better capitalized and have a higher proportion of investment grade ratings versus non-investment grade ratings, the latter of which are

²² For example, among the questions included in the Due Diligence Framework is whether "safeguards should be put in place to ensure that the NAIC does not violate the Credit Rating Agency Reform Act." Due Diligence Framework at page 16.



expected to have higher rates of transition and default. These higher rates of transition and default are not an indication of the quality of the CRP's ratings, but rather a reflection of universe of lower capitalized entities the CRPs rate. The Due Diligence Framework should not operate to penalize newer CRPs on this basis but should instead incorporate consideration of this inherit bias. To the extent the Due Diligence Framework seeks to demonstrate from an analytical perspective that credit ratings can be used as a proxy for NAIC Designations, it must leverage an appropriate sample size that excludes bias (such as only looking at cases where the NAIC chose to evaluate a security, versus the thousands of instances where it accepted a rating).

Finally, the Due Diligence Framework must be transparent in order to be analytically credible and to mitigate perceptions of more widespread bias in favor of incumbent CRPs. Recent NAIC initiatives²³ and research publications²⁴ provide limited insight into the NAIC's own analytical process yet signal skepticism toward CRPs, particularly CRPs that may be newer or smaller than incumbent CRPs. This not only does a disservice to the impacted CRPs, but it also calls into question the value of the process and the veracity of the results. To build market trust, confidence, and credibility, the Due Diligence Framework should adhere to higher standards and offer the same level of transparency as the CRPs it aims to assess.

²³ The NAIC Financial Condition (E) Committee recently adopted the recommendation of its Valuation of Securities (E) Task Force to establish a process that allows NAIC Investment Analysis Office discretion to assign its own NAIC designation in place of the NAIC designation derived from the credit rating assigned by a CRP through the filing-exempt process (the "SVO Discretion Process"). As noted in our comment letter to NAIC on the SVO Discretion Process, unlike CRPs which publish their credit rating methodologies and publicly disclose detailed information about their analytical process, the SVO Discretion Process provides few details about the SVO Credit Committee review process and the factors it will consider as part of its assessment. See KBRA Letter to NAIC dated July 26, 204 ("Revised Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the "P&P Manual") Authorizing the Procedures for the SVO's Discretion Over NAIC Designations Assigned Through the Filing Exemption Process").

²⁴ See NAIC Capital Markets Bureau Special Report: *Growth in Private Ratings Among U.S. Insurer Bond Investments and Credit Rating Differences* (May 2024).



Annex II

Overview of Existing SEC Requirements for NRSROs

In accordance with federal law and SEC rules,²⁵ NRSROs are required to:

- File with the SEC an annual certification of its Form NRSRO registration,²⁶ promptly update its filing in certain circumstances,²⁷ and make its current Form NRSRO filing and most of its current Form NRSRO Exhibits available on its public website.²⁸
- Disclose certain information, including information concerning the NRSRO's performance measurement statistics and its procedures and methodologies to determine ratings.²⁹
- Establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings,³⁰ and retain records of its internal control structure.³¹
- Consider certain factors with respect to its establishment, maintenance, enforcement, and documentation of an effective internal control structure.³²
- Establish, maintain, enforce, and document policies and procedures reasonably designed to achieve certain objectives concerning its development and application of, and disclosures related to, methodologies and models.³³
- File an unaudited report containing an assessment by management of the effectiveness during the fiscal year of the NRSRO's internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings.³⁴ The report must be accompanied by a signed statement by the NRSRO's chief executive officer or an individual performing similar functions.³⁵
- Establish, maintain, enforce, and document policies and procedures that are reasonably designed to: assess the probability that an issuer of a security or money market instrument will default or fail to make required payments to investors,³⁶ and ensure that it applies any rating symbol,

²⁵ Appendix: Summary of Statutory Framework and Rules, SEC Office of Credit Ratings Staff Report on Nationally Recognized Statistical Rating Organizations (February 2024), available at <https://www.sec.gov/files/feb-2024-ocr-staff-report.pdf>.

²⁶ Section 15E(b)(2) and Rule 17g-1(f).

²⁷ Section 15E(b)(1) and Rule 17g-1(e).

²⁸ Section 15E(a)(3) and Rule 17g-1(i).

²⁹ Section 15E(a)(1)(B)(i) and Section 15E(a)(1)(B)(ii).

³⁰ Section 15E(c)(3)(A).

³¹ SEC Rule 17g-2(b)(12).

³² See, e.g., SEC Rule 17g-8(d)(1)–(4).

³³ See, e.g., SEC Rule 17g-8(a)(2)–(5).

³⁴ SEC Rule 17g-3(a)(7)(i).

³⁵ SEC Rule 17g-3(b)(2).

³⁶ SEC Rule 17g-8(b)(1).

number, or score in a manner that is consistent for all types of obligors, securities, and money market instruments for which the symbol, number, or score is used.³⁷

- Publish an information disclosure form when taking a rating action with respect to a rating assigned to an obligor, security, or money market instrument in a class for which it is registered as an NRSRO.³⁸ The information form must disclose certain information with respect to the particular rating action.³⁹ In addition, the NRSRO must attach to the information disclosure form a signed statement by a person within the NRSRO with responsibility for the rating action.⁴⁰
- Make and retain, or retain, certain records, including a record documenting its established procedures and methodologies used to determine credit ratings⁴¹ and records related to its ratings.⁴² An NRSRO must promptly furnish to the SEC or its representatives copies of required records, including English translations of those records, upon request.⁴³
- Establish, maintain, and enforce written policies and procedures reasonably designed to prevent the misuse of material non-public information (“MNPI”), including the inappropriate dissemination of MNPI both within and outside the NRSRO, the inappropriate trading of securities using MNPI by a person within the NRSRO, and the inappropriate dissemination of pending credit rating actions within and outside the NRSRO before issuing the rating on the Internet or through another readily accessible means.⁴⁴
- Establish, maintain, and enforce written policies and procedures reasonably designed to address and manage conflicts of interest.⁴⁵ Certain conflicts of interest are expressly prohibited,⁴⁶ and for other types of conflicts of interest, the NRSRO must disclose the conflicts and have policies and procedures in place to manage them.⁴⁷
- Refrain from engaging in specified unfair, coercive, or abusive practices.⁴⁸
- Provide information on whether it has in effect a code of ethics, and if not, the reasons it does not have a code of ethics.⁴⁹

³⁷ SEC Rule 17g-8(b)(3).

³⁸ SEC Rule 17g-7(a).

³⁹ SEC Rule 17g-7(a)(1)(ii)(A)-(N) specifies the information that must be disclosed in the information disclosure form.

⁴⁰ Rule 17g-7(a)(1)(iii).

⁴¹ Rule 17g-2(a)(6).

⁴² SEC Rule 17g-7(a)(1)(iii).

⁴³ SEC Rule 17g-2(a)(6).

⁴⁴ The records that an NRSRO must make and retain, or retain, with respect to its ratings include the identity of certain persons who participated in determining or approving the rating, records used to form the basis of a rating, external and internal communications received or sent by the NRSRO and its employees related to a rating, and for ABS ratings, a record of the rationale for any material difference between the final rating assigned and the rating implied by a quantitative model that was a substantial component in determining the rating. SEC Rule 17g-2(a)(2)(i), (ii), and (iii); SEC Rule 17g-2(b)(2) and (b)(7).


⁴⁵ Section 15E(a) and (b) and SEC Rule 17g-2(f).

⁴⁶ Section 15E(g) and SEC Rule 17g-4.

⁴⁷ Section 15E(h) and SEC Rule 17g-5.

⁴⁸ SEC Rule 17g-5(c).

⁴⁹ SEC Rule 17g-5(a)(1) and (a)(2); SEC Rule 17g-5(b).

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- Establish procedures for the receipt, retention, and treatment of complaints regarding credit ratings, models, methodologies, and compliance with the securities laws and its policies and procedures developed under this regulatory regime, and of confidential, anonymous complaints.⁵⁰
 - Designate a compliance officer (the “DCO”) responsible for administering policies and procedures related to MNPI and conflicts of interest, ensuring compliance with the securities laws and regulations, and establishing procedures for handling complaints by employees or users of credit ratings.⁵¹ The DCO must submit an annual report to the NRSRO on the compliance of the NRSRO with the securities laws and the NRSRO’s policies and procedures, and the NRSRO must file the report with the SEC.⁵²
 - Maintain a board of directors or similar governing body (collectively, “the Board”), certain of whose members must be independent from the NRSRO.⁵³ An NRSRO’s Board, or members thereof, are responsible for exercising oversight of specified subjects related to the NRSRO’s rating business and for approving the procedures and methodologies, including qualitative and quantitative data and models, that the NRSRO uses to determine ratings.⁵⁴
 - Establish, maintain, enforce, and document standards of training, experience, and competence for the individuals it employs to participate in the determination of credit ratings that are reasonably designed to achieve the objective that the NRSRO produces accurate credit ratings, and retain a record of these standards.⁵⁵
 - Establish policies and procedures regarding post-employment activities of certain former personnel.⁵⁶

⁵⁰ SEC Rule 17g-6.

⁵¹ Section 15E(j)(1) and (3).

⁵² Section 15E(j)(5).

⁵³ Section 15E(t)(2).

⁵⁴ Section 15E(t)(3) and Rule 17g-8(a)(1)

⁵⁵ SEC Rule 17g-9.

⁵⁶ Section 15E(h)(4) and (5); Rule 17g-8(c).

October 14, 2024

Via Email (DDaveline@naic.org)

Commissioner Nathan Houdek, Chair
Financial Condition (E) Committee
National Association of Insurance Commissioners
1100 Walnut Street, Suite 500
Kansas City, MO 64106-2197

Re: Draft Request for Proposal – Credit Rating Provider Due Diligence Framework

Dear Commissioner Houdek,

Moody's Ratings ("Moody's") appreciates the opportunity to provide comments on the National Association of Insurance Commissioners' ("NAIC") *Draft Request for Proposal – Credit Rating Provider Due Diligence Framework* ("RFP"), which was released for comment by the NAIC's Financial Condition (E) Committee ("E-Committee") on August 15, 2024.

Moody's values the NAIC's ongoing commitment to transparency in implementing the recommendations from the E-Committee's *Framework for Regulation of Insurer Investments – A Holistic Review*. This includes the recommendation to engage a third-party consultant to design and to help implement a robust due diligence framework ("DDF") for the NAIC's continued use of credit rating providers ("CRPs"), while retaining the overall utilization of CRP ratings.

Moody's supports the NAIC's effort to develop the DDF and recommends that the DDF focus on reviewing the mappings used by the NAIC in the "filing exempt" process to translate the ratings of individual CRPs to NAIC Designations¹. This review should include consideration of how mappings between ratings of individual CRPs and NAIC Designations might vary across sectors – such as between corporate and structured finance obligations, between public and private ratings, or between securities rated by a single CRP and those rated by multiple CRPs.

For this initiative, we recommend that the DDF focus on analyzing the following key data elements:

- CRP-provided rating definitions, methodologies, and default and loss studies;

¹ As this term is defined in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* ("P&P Manual").

- Ratings assigned by CRPs to three distinct categories: (i) securities publicly rated by two or more CRPs; (ii) securities publicly rated by only one CRP, and (iii) securities that only carry private letter ratings; and
- Insights gleaned from state insurance supervisory examinations that focus on the utilization of CRP ratings in insurers' investment decision-making and risk management processes.

Additionally, we offer recommendations on the selection process and assessment criteria for third-party consultants.

I. Due Diligence Process Should Focus on Mapping CRP Ratings to NAIC Designations While Taking into Account Sector Variations

The draft RFP states that a Nationally Recognized Statistical Rating Organization (“NRSRO”) applying to become a CRP currently provides its own mapping of NRSRO ratings to corresponding NAIC Designations. Additionally, the RFP states that the NAIC would like to utilize data to validate CRP mappings and/or establish its own ratings mapping.

We concur with the NAIC that there should be an independent review and validation of the rating mappings provided by NRSROs to ensure full alignment with NAIC Designations. We also support the development of the NAIC's own methodology for ratings mapping, both broadly and within specific investment classes. We believe that mapping NRSRO ratings to NAIC Designations should play a central role in the DDF and take precedence over scrutinizing the NRSRO's policies, procedures and internal controls, as this area is already reviewed during the annual NRSRO examinations conducted by the U.S. Securities and Exchange Commission.

While CRPs typically provide a single mapping from their ratings to NAIC Designations, it may be beneficial for the NAIC to explore alternative mappings for different sectors. Such mappings could prove more suitable for certain asset classes. Differential treatment of private letter ratings may also be appropriate in sectors where a CRP has issued a limited number of public ratings on securities that were also rated by other CRPs, thus lacking broader market scrutiny and the implicit validation of the rating levels typically afforded to publicly assigned ratings. Finally, ratings on securities that carry a rating from only one CRP may also merit differential mapping, particularly in structured finance where different CRPs may be asked to rate different tranches of a single securitization, which may be indicative of “rating shopping.”

II. CRP Rating Definitions and Other Data Elements

In developing a ratings mapping methodology, we recommend that the NAIC review data published by each CRP – including rating definitions, methodologies, and default and loss studies. In addition, for a more comprehensive understanding, the DDF should provide for a review of both the ratings currently assigned by the CRPs and insights gained from the state insurance supervisory examination process regarding the insurers' use of CRP ratings.

To establish and maintain mappings between CRP ratings and NAIC Designations, the NAIC should consider including as part of the DDF an assessment of the comparability of individual CRP's rating scales and NAIC Designations. In a broad sense, a score derived from one scale may indicate a different level of investment risk (as defined below), on average, than a similar score from another scale. In addition, the NAIC may wish to consider using different maps in asset classes where a CRP's rating definition incorporates loss-given-default, "tail risk," or investment horizon differently than intended by the NAIC in its Designations.

Loss Given Default ("LGD"). NAIC Designations represent opinions of gradations of the likelihood of an insurer's timely receipt of an investment's full principal and expected interest ("investment risk"). Where appropriate for a given investment, NAIC Designations and NAIC Designation Categories² will reflect "tail risk" and/or LGD, the position of the specific liability in the issuer's capital structure, and all other risks, except for volatility/interest rate, prepayment, extension or liquidity risk.

In developing a rating mapping methodology, the NAIC should consider examining how each CRP incorporates a security's expected LGD into their methodologies to assign ratings in each major asset class and assess whether adjustments to the mapping are necessary. For instance, if two CRPs align in their rating scales with respect to default probability but diverge in their treatment of LGD for structured finance securities, it is likely that ratings for the same security tranche would not correspond to an identical NAIC Designation. Based on the CRP's sectoral rating definitions, applicable rating methodologies, and the definitions of NAIC Designations and NAIC Designation Categories, the NAIC may consider adjusting a CRP's rating up or down in its mapping to better align with the corresponding NAIC Designation Category.

"Tail Risk." The current version of the P&P Manual leaves the definition of "tail risk" unspecified, leading to ambiguity in its application to NAIC Designations. Should "tail risk" refer to expected LGD, inclusive of expected LGD for mezzanine structured finance securities, the NAIC's ratings mapping methodology should reflect this interpretation. Alternatively, if "tail risk" encompasses systemic risk – indicating a higher likelihood of default when other securities are also defaulting – it should be noted that this aspect is typically not included in CRPs' rating definitions. Consequently, systemic risk might be more appropriately addressed through asset-level risk-based capital charges rather than being integrated into NAIC Designations.

Investment Horizon. When mapping CRP ratings to NAIC Designations, it is important to consider how each CRP incorporates maturity into its ratings and how the NAIC intends to factor maturity into its Designations. The current version of the P&P Manual is not explicit about how the risks associated with varying investment horizons (or remaining terms to maturity) should be reflected in NAIC Designations. All else being equal, investment risk rises with maturity due to the increasing likelihood of default and loss over time. Some CRPs, however, assign a single rating, independent of maturity, to all securities issued by an individual obligor. In practice, NAIC Designations also appear to be horizon-free; *i.e.*, not impacted by an obligation's term to maturity. In contrast, the intrinsic price approach employed by the NAIC's Investment Analysis Office in evaluating

² As this term is defined in the P&P Manual.

mortgage-backed securities appears to provide more favorable capital treatment for short-term securities than for long-term securities.

Rating Methodologies. Comparing rating methodologies across CRPs assigning ratings in a given sector may allow the NAIC to infer whether one of the CRPs would tend to rate issuers in that sector systematically higher or lower than other CRPs. A careful review of CRP methodologies may be most beneficial in situations in which direct rating comparisons are most difficult, such as sectors where only a few CRPs have assigned a large number of public ratings.

Default and Loss Studies. Comparisons of the default and loss experience associated with the rating levels assigned by different CRPs merit close attention within the DDF. There are a few caveats, however, that should be considered before drawing broad conclusions from this data source. A substantial portion of insurance company investments in debt securities is classified under NAIC Designations as investment-grade. In the investment-grade part of the rating scales — where defaults are likely to be infrequent — default studies might not provide a sufficient foundation for evaluating the quality and compatibility of CRP ratings with NAIC Designations. The occurrence or absence of defaults can be idiosyncratic, potentially obscuring broader systemic performance issues. Furthermore, given that CRPs periodically adjust their rating methodologies, relying on past performance may not accurately predict future performance.

Average Rating Differences. Conversely, differences between the average ratings assigned by two or more CRPs to the same securities are likely to be a strong indicator of differences in future default rates by rating category. Regardless of observed differences in historical rating performance, if one CRP systematically assigns higher (or lower) ratings than another CRP in a particular sector or universally, then the first CRP is likely to experience higher (or lower) default rates by rating category in that sector or overall. However, average rating differences (or similarities) observed on securities that are rated publicly by two or more CRPs may not be predictive of expected relative default experience for securities that either carry only private letter ratings or are publicly rated by a single CRP. This discrepancy can occur because the differences in average ratings observed among jointly rated public securities may not extend to: (a) private letter ratings given the lack of public market scrutiny and market discipline, and (b) public ratings assigned by a single CRP due to the greater vulnerability of single-CRP-rated securities to rating inflation potentially arising from “rating shopping.”

III. Insights Gained from Supervisory Examinations

In our October 9, 2023 comment letter to the NAIC, we recommended that the NAIC consider enhancing its oversight of insurers’ asset underwriting and internal risk management practices. We specifically recommended expanding the scope, depth and frequency of such oversight to reduce incentives for potential regulatory capital arbitrage and “rating shopping.” We proposed that this enhanced oversight include having insurers establish effective controls for selecting and using CRPs for credit risk management within their portfolios, with a particular focus on the controls governing the use of private letter ratings. We would like to reassert this recommendation and further highlight the need to assess the consistency in how insurers apply ratings from specific CRPs in the

“filing exempt” process, underwriting, and risk management.

Furthermore, we recommend that the insurer oversight process include a mechanism for collecting and analyzing findings related to supervisory reviews of the insurers’ use of CRP ratings. It is recommended that these findings be systematically reported to the appropriate governance groups within the NAIC. An understanding of how different insurers map ratings from different CRPs to their own internal risk scores could help inform the NAIC’s mappings.

IV. Third-Party Consultant Selection Process and Assessment Criteria

1. Consultant Conflicts of Interest Management

The draft RFP requires respondents to disclose all conflicts of interest, sign a Conflict-of-Interest Form specific to NAIC relations, and adhere to policies for managing these conflicts, with NAIC leadership’s approval. To enhance these requirements, we believe the RFP should expand the scope of the Conflict-of-Interest Form to cover broader conflict-of-interest scenarios and require the third-party consultant to establish internal controls, such as audits, training, and transparent reporting, to strengthen compliance and management of conflicts of interest. Additionally, we recommend that the NAIC evaluate prohibiting conflicts of interest resulting from the consultant’s direct or indirect affiliations with NRSROs, the insurance sector, and asset managers linked to insurance firms or NRSROs, as well as personal or financial ties that could impair the consultant’s objectivity and decision-making integrity.

2. Consultant Information Requests to CRPs

If the NAIC anticipates that the consultant will engage with CRPs as part of developing recommendations for the DDF, we recommend that the RFP require the consultant to describe the process for soliciting and securely storing information from CRPs and how such information would be used by the consultant and incorporated into the DDF. Additionally, the consultant’s response should address any potential legal limitations they might encounter in gathering and using such information, including confidentiality restrictions, and how these limitations can be overcome.

* * *

We look forward to continued engagement with the NAIC on these topics and welcome the opportunity to discuss these issues with you in greater detail.

Sincerely,

/S/ Nick Miller

Nick Miller
Managing Director – Global Regulatory Affairs

THE LEASE-BACKED SECURITIES WORKING GROUP

To: Commissioner Houdek (WI), Chair of the Financial Condition (E) Committee

From: The Lease-Backed Securities Working Group

Re: Request for Comments on the Draft Request for Proposal

Date: October 14, 2024

Commission Houdek:

This letter is in response to the request for comments on the Draft Request for Proposal that was exposed at the August 2, 2024 meeting of the Financial Conditions (E) Committee.

Our group, The Lease-Backed Securities Working Group, is fully supportive of a robust due-diligence process for NAIC Credit Ratings Providers (“CRP”s) in accordance with the principles laid out in the *Framework for Regulation of Insurer Investments – A Holistic Review*. We believe that a well-designed due-diligence process should not only enhance the tools available to the SVO, but also lead to greater clarity and predictability for market participants.

Our comments are very simple, and are limited to the “Objectives” portion of the request for comment, specifically: “(2) Are there additional objectives that we should consider that are not included here?”

In the “Vision and Objectives” section of the RFP itself, it lists off the following three objectives (summarizing for brevity):

- Reduce/eliminate “blind” reliance on CRP ratings but retain over-all utilization of CRPs ratings.....
- [The creation of] a quantitative and qualitative due-diligence framework design....
- Retain ability within the SVO to perform individualized credit assessment when needed..... [which discretion would ideally] be rarely used if other governance is optimized.

We would suggest that the inclusion of a global objective would be helpful – whether before or in addition to the ones listed above -- along the lines of:

“The CRP framework should be designed in such a way that -- when implemented -- it will both enhance the ability of the SVO to analyze investment risk, and also result in increased clarity and predictability for market participants as they interface with the NAIC and the SVO.”

It could be said that such an objective is assumed and doesn’t need to be stated explicitly, however we believe that including such a basic statement would be beneficial.

THE LEASE-BACKED SECURITIES WORKING GROUP

Specifically, a robust and clear due-diligence framework would assist market participants in understanding the conditions under which “Filing Exemption” is the appropriate for a given security – and when it is not.

The framework should also assist market participants in understanding and being able to anticipate the rare situations in which the SVO would be likely to exercise its discretion to perform “individualized credit assessments” for otherwise-eligible Filing-Exempt securities – whether that is because there are additional “investment risks” over and above “credit risk” – or because of a specific disagreement with the “credit risk” assessment of a CRP.

In other words, adding a stated objective to the effect that the proposed framework should not only enhance the NAIC’s ability at assess investment risk, but also provide greater clarity and predictability to investors in their interactions with the NAIC, would be – we think – a simple, but useful, addition to the RFP.

We thank you for considering our comments.

John Garrison

On behalf of The Lease-Backed Securities Working Group.