

*Conference Call*

**VALUATION OF SECURITIES (E) TASK FORCE**

**Thursday, February 18, 2020**

**3:00 p.m. – 4:00 p.m. ET / 2:00 p.m. – 3:00 p.m. CT / 1:00 p.m. – 2:00 p.m. MT / 12:00 pm. – 1:00 p.m. PT**

**ROLL CALL**

Dana Popish Severinghaus, Chair	Illinois	Gary Anderson	Massachusetts
Doug Ommen, Vice Chair	Iowa	Chlora Lindley-Myers	Missouri
Lori K. Wing-Heier	Alaska	Bruce R. Range	Nebraska
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David Altmaier	Florida	Doug Slape	Texas
Dean L. Cameron	Idaho	Jonathan T Pike	Utah
Vicki Schmidt	Kansas	Scott A. White	Virginia
James J. Donelon	Louisiana	Mike Kreidler	Washington
Kathleen A Birrane	Maryland	Mark Afable	Wisconsin

NAIC Support Staff: Charles A. Therriault, Marc Perlman

**AGENDA**

1. Receive a Proposed Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual) to Update the Financial Modeling Instructions for RMBS/CMBS Securities and Direct IAO Staff to Produce NAIC Designation and NAIC Designations Categories for Non-Legacy Securities  
(Doc. ID 2021-027.01)  
—Kevin Fry (IL), Eric Kolchinsky (NAIC), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment A
2. Discuss Comments Received and Consider for Adoption a Proposed Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual) to Require the Filing of Private Rating Letter Rationale Report  
(Doc. ID 2020-023.02, 2020-023.03)  
—Kevin Fry (IL), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment B & B - 1
3. Receive Referral from the Statutory Accounting Principles (E) Working Group on Non-conforming Credit Tenant Loans  
(Doc. ID 2021-029.01, 2021-029.02, 2021-029.03)  
—Kevin Fry (IL), Eric Kolchinsky (NAIC), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment C, C – 1 & C - 2
4. Receive a Proposed Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual) to Update the List of NAIC Credit Rating Providers to Reflect NRSRO Changes  
(Doc. ID 2021-028.01)  
—Kevin Fry (IL), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment D

5. Discuss U.S. Securities Exchange Commission (SEC) Rule 18f-4 Under the Investment Company Act of 1940 Related to the Use of Derivatives by Registered Investment Companies  
—Kevin Fry (IL), Charles Therriault (NAIC), Marc Perlman (NAIC)
6. Any other matters

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**MEMORANDUM**

TO: Kevin Fry, Chair, Valuation of Securities (E) Task Force  
Members of the Valuation of Securities (E) Task Force

FROM: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)  
Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

CC: Marc Perlman, Investment Counsel, NAIC Securities Valuation Office (SVO)

RE: Proposed Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual)* to Update the Financial Modeling Instructions for RMBS/CMBS Securities and Direct IAO Staff to Produce NAIC Designation and NAIC Designations Categories for Non-Legacy Securities

DATE: February 03, 2021

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**1. Summary** – On Oct. 11, 2018, the Valuation of Securities (E) Task Force adopted an amendment to delete the Modified Filing Exempt (MFE) provisions from the P&P Manual and directed a referral to the Statutory Accounting Principles (E) Working Group recommending the deletion of the MFE provisions from Statement of Statutory Accounting Principles (SSAP) No. 43R—Loan-Backed and Structured Securities. The effect of these changes resulted in these securities coming under the filing exempt instructions in the P&P Manual, if they have an Eligible NAIC CRP Credit Rating assigned to them. This change eliminated using the book adjusted carrying value to determine the NAIC designation for these securities.

The IAO staff reported to the Task Force at the 2019 Summer National Meeting that at some point the NAIC should align the RMBS/CMBS modeling to provide a single NAIC Designation for modeled RMBS/CMBS. This would have been a change from the current practice of providing a series of book adjusted carrying value price breakpoints to companies to determine the NAIC designation. The IAO staff submitted a proposal to the Task Force at the 2019 Fall National Meeting to eliminate the book adjusted carrying value price breakpoint process but the Task Force decided at the Feb. 4, 2020 meeting to defer such a change because industry expressed concerns there would be significant adverse risk-based capital (RBC) consequences from making such a change at that time.

In March 2020, the impact from the pandemic was just beginning to become apparent in the U.S. The pandemic's effect on RMBS and CMBS securities became more observable during the 2020 year-end financial modeling process. The 2020 year-end financial modeling identified several securities that no longer qualified as being zero-loss because more conservative scenarios, necessary to reflect the economic impact of the pandemic, were applied. Once these securities no longer qualified as being zero-loss, they became subject to the book adjusted carrying value price breakpoints process. Many of these securities are owned at a significant premium because of the low interest rate environment and, once the price break points were applied, securities that would otherwise be considered very high

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quality were required to be reported as an NAIC 2, 3, or 4 just because of their book adjusted carrying value and not because of any credit concern.

At the Task Force's Dec. 18, 2020 meeting, industry, represented by the ACLI, agreed with the IAO staff that the mechanics of the price break points was causing insurer owned securities with otherwise strong credit to be reported as NAIC 2, NAIC 3 and NAIC 4 under the financial modeling price breakpoints process purely because they are owned at a premium and not because of their credit risk. It was also discussed that the use of financial modeling price breakpoints process was possibly disrupting the market for these otherwise high-quality investments. SSG staff at that meeting recommended getting rid of the price breakpoints process.

**2. Recommendation** – The IAO staff recommends that the NAIC move to a single NAIC designation and NAIC designation category for all non-Legacy Securities (those financially modelled RMBS/CMBS securities that closed on or after to Jan. 1, 2013). Moving away from financial modeling price breakpoints process for these non-Legacy Securities will avoid further and future market disruptions and permit a clearer assessment of the credit risk assessment for these securities that will not be impacted by the insurers book adjusted carrying value. Making this change for only non-Legacy Securities preserves their historical treatment. Given the potential impact to SSAP 43R - *Loan-Backed and Structured Securities*, staff recommends a referral to the Statutory Accounting Principles (E) Working Group.

**3. Proposed Amendment** – The following text shows the revisions in Part Four that would appear in the 2020 P&P Manual format.

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**PART FOUR**  
**THE NAIC STRUCTURED SECURITIES GROUP**

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## DEFINITIONS

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1. The following terms used in this Part Four have the meaning ascribed to them below.
  - **ABS** stands for asset-backed securities and means structured securities backed by consumer obligations originated in the United States.
  - **CMBS** stands for commercial mortgage-backed securities and means structured securities backed by commercial real estate mortgage loans originated in the United States. The definition of CMBS may refer to securitizations backed by commercial mortgages, respectively, originated outside of the United States if and to the extent that the vendor selected by the NAIC to conduct the financial modeling: (a) has the necessary information about the commercial mortgage and commercial mortgage loans originated outside of the United States to fully model the resulting securities; and (b) can adapt the modeling process to account for any structural peculiarities associated with the jurisdiction in which the mortgage was originated.
  - **Initial Information** means the documentation required to be filed with an Initial Filing of an RMBS or a CMBS CUSIP, pursuant to the section below and pertaining to Loan Information, Reps and Warranty Information and Structure and Formation Information for the transaction, where:
    - *Loan Information* means a review of the loan files by a third party to assess the sufficiency of legal title and other related issues.
    - *Reps and Warranty Information* means the actual representation and warranties in effect for the securitization given by the mortgage originator(s) to the Trust pertaining to loan origination processes and standards, compliance with applicable law, loan documentation and the process governing put backs of defective mortgages back to the originator(s).
    - *Structure and Formation Information* means the waterfall, as described in the definition of Ongoing Information, information and documentation in the form of legal opinions and documentation governing the formation of the securitization and its entities relative to issues such as bankruptcy remoteness, true sale characterization, the legal standards and procedures governing the securitization and other similar issues.
  - **Intrinsic Price** is an output of financial modeling, defined as ‘1 - weighted average of discounted principal loss’ expressed as a percentage, reflecting the credit risk of the security.

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- **Legacy Security**, for the purposes of this section shall mean any RMBS and any CMBS that closed prior to January 1, 2013.
- **Official Price Grids** means and refers to those generated by the SSG and provided to an insurance company or insurance companies that own the security for regulatory reporting purposes.
- **Ongoing Information** consists of: (a) tranche level data; such as principal balance, factors, principal and interest due and paid, interest shortfalls, allocated realized losses, appraisal reductions and other similar information for the specific tranche; (b) trust level data, such as aggregate interest and principal and other payments received, balances and payments to non-tranche accounts, aggregate pool performance data and other similar information; (c) loan level performance information; and (d) a computerized model of rules that govern the order and priority of the distribution of cash from the collateral pool (i.e., the “waterfall”) to the holders of the certificates/securities—provided in the format and modeling package used by the NAIC financial modeling vendor.
- **Original Source**, with respect to a specific set of data, means the Trustee, Servicer or similar entity that is contractually obligated under the agreement governing the RMBS or CMBS to generate and maintain the relevant data and information in accordance with standards specified in applicable agreements or an authorized re-distributor of the same.
- **NAIC Designation Intrinsic Price Mapping** is the mapping of the Intrinsic Price to a single NAIC Designation and Designation Category employing the midpoints between each adjoining AVR RBC charges (pre-tax). The midpoints are directly used as the minimum Intrinsic Prices (weighted average loss points) for corresponding NAIC Designations and Designation Categories.
- **Price Grids** means and refers to CUSIP-specific price matrices containing six price breakpoints; i.e., each price corresponding to a specific NAIC Designation category. Each breakpoint on a Price Grid is the price point that tips the NAIC Designation for the RMBS CUSIP into the next NAIC Designation (credit quality/credit risk) category. The plural is used because two Price Grids are generated for any CUSIP. This reflects the difference in RBC for those insurance companies that maintain an asset valuation reserve and for those insurance companies that do not.

- **Re-REMIC** is a securitization backed by: (a) otherwise eligible RMBS from one or two transactions; or (b) otherwise eligible CMBS from one or two transactions at closing. Re-REMICs cannot acquire any Underlying Securities after closing.
- **RMBS** stands for residential mortgage-backed securities and means structured securities backed by non-agency residential mortgages originated in the United States, where the collateral consists of loans pertaining to non-multi-family homes. That includes prime, subprime and Alt-A mortgages, as well as home-equity loans, home-equity lines of credit and Re-REMICs of the above. Excluded from this definition is agency RMBS, where the mortgages are guaranteed by federal and federally sponsored agencies such as the Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA) or Federal Home Loan Mortgage Corporation (FHLMC) and loans against manufactured or mobile homes or collateralized debt obligations backed by RMBS. The exclusion covers bonds issued and guaranteed by, or only guaranteed by, the respective agency. Also not included are loans guaranteed by the U.S. Department of Veteran Affairs or the U.S. Department of Agriculture’s Rural Development Housing and Community Facilities Programs. The definition of RMBS may refer to securitizations backed by residential mortgages, respectively, originated outside of the United States if and to the extent that the vendor selected by the NAIC to conduct the financial modeling: (a) has the necessary information about the residential mortgage and residential mortgage loans originated outside of the United States to fully model the resulting securities; and (b) can adapt the modeling process to account for any structural peculiarities associated with the jurisdiction in which the mortgage was originated.
- **Underlying Security** means the RMBS or CMBS backing a Re-REMIC. A Re-REMIC cannot be an Underlying Security.

**NOTE:** The definitions of RMBS and CMBS reflect limitations associated with the financial modeling process, NAIC credit rating provider (CRP) internal naming conventions and SSG processes, as more fully discussed below and may, therefore, be subject to a narrower or a broader reading in any reporting period. Please call the SSG with any concerns or questions about the scope of the definitions for a given reporting period. Also note:

- It is possible that the scope of the RMBS and CMBS definitions may be broadened because the financial modeling vendors indicate other collateral or waterfall structures can be modeled.

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- NAIC CRPs may adopt different internal conventions with respect to what market or asset segments are within their rated populations of RMBS, CMBS or ABS. This could affect the application of the adopted NAIC methodology or require the NAIC to select which naming process it wishes to adopt.
- It is possible that the SSG will acquire analytical assessment capabilities that permit the assessment of existing, additional or different structured securities that cannot now be modeled or that are not currently rated.

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## ADMINISTRATIVE AND OPERATIONAL MATTERS

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### Certain Administrative Symbols

2. The following administrative symbols are used in the Valuation of Securities (VOS) Products to identify RMBS and CMBS that the NAIC vendor has confirmed will be subject to the financial modeling methodology described in this Part.
  - **FMR** – Indicates that the specific CUSIP identifies a **Legacy Security** RMBS that is subject to the financial modeling methodology **and the application of Price Grids to determine a NAIC Designation and Designation Category**.
  - **FMC** – Indicates that the specific CUSIP identifies a **Legacy Security** CMBS that is subject to the financial modeling methodology **and the application of Price Grids to determine a NAIC Designation and Designation Category**.
  - **FSR** – Indicates that the specific CUSIP identifies a **non-Legacy Security** RMBS that is subject to the financial modeling methodology and assignment of a NAIC Designation and Designation Category by the SSG.
  - **FSC** – Indicates that the specific CUSIP identifies a **non-Legacy Security** CMBS that is subject to the financial modeling methodology and assignment of a NAIC Designation and Designation Category by the SSG.

**NOTE:** The administrative symbols **FMR**~~and~~, **FMC**, **FSR** and **FSC** are related to symbols that insurers are required to use in the financial statement reporting process. Under applicable financial statement reporting rules, an insurer uses the symbol **FM** as a suffix to identify **Legacy Security** modeled RMBS and CMBS CUSIPs **and FS** as a suffix to identify **non-Legacy Security** modeled RMBS and CMBS CUSIPs. The symbol **FM** or **FS** is inserted by the insurer in the financial statement as a suffix following the NAIC Designation **C**category; e.g., **2.B FM**, **3.C FS**.

The use of these administrative symbols in the VOS Product means the insurer should not use the filing exempt process for the security so identified.

### Quarterly Reporting of RMBS and CMBS

3. To determine the NAIC Designation to be used for quarterly financial statement reporting for an RMBS or CMBS purchased subsequent to the annual surveillance described in this Part, the insurer uses the prior year-end modeling data for that CUSIP (which can be obtained from the NAIC) and follows the instructions in contained under the heading “Use of Net Present Value and Carrying Value for Financially Modelled Legacy Security RMBS and CMBS” ~~below~~ or ~~follows the instructions in~~ “~~Publication of Final Results Use of Intrinsic Price for Financially Modeled non-Legacy Security RMBS and CMBS~~” below, subject to, and in accordance with, *SSAP No. 43R—Loan-Backed and Structured Securities*.

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## FILING EXEMPTIONS

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### Limited Filing Exemption for RMBS and CMBS

4. **RMBS and CMBS that Can be Financially Modeled** – RMBS and CMBS that can be financially modeled are exempt from filing with the SVO. NAIC Designations for RMBS and CMBS that can be financially modeled are determined by application of the methodology discussed in this Part, not by the use of credit ratings of CRPs.
5. **RMBS and CMBS securities that Cannot be Financially Modeled**
  - **But Are Rated by a CRP** – RMBS and CMBS that cannot be financially modeled but that are rated by a CRP are exempt from filing with the SSG. The NAIC Designations for these RMBS and CMBS are determined by application of the filing exemption procedures discussed in this Manual.
  - **But Are Not Rated by a CRP** – RMBS and CMBS that cannot be financially modeled and that are not rated by a CRP are not filing exempt and must be filed with the SSG or follow the procedures, as discussed below in this Part.

### Filing Exemption for ABS

6. ABS rated by a CRP are exempt from filing with the SSG.

### Review of Decisions of the SSG

7. Analytical decisions made through the application of financial modeling are not subject to the appeal process. In the absence of an appeal, the SSG shall provide whatever clarification as to the results of financial modeling is possible to any insurer who requests it and owns the security, provided that it is not unduly burdensome for the SSG to do so. Any decision made by the SSG that results in the assignment of an NAIC Designation and does not involve financial modeling methodology, whether developed by the SSG on its own or in collaboration with the SVO, is subject to the appeal process.

## **REQUIRED DATA AND DOCUMENTS FOR TRANSACTIONS SUBMITTED TO THE SSG**

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8. The policy statement set forth in this section shall be applicable generally to any transaction filed with the SSG for an analytical assessment, including, but not limited to, a Price Grid or for assignment of an NAIC **Designation**. Any filing with the SSG is deemed to be incomplete unless the insurer has provided the information, documentation, and data in quantity and quality sufficient to permit the SSG to conduct an analysis of the creditworthiness of the issuer and the terms of the security to determine the requested analytical value. It is the obligation of the reporting insurance company to provide the SSG with all necessary information. It is the responsibility of the SSG to determine whether the information provided is sufficient and reliable for its purposes and to communicate informational deficiencies to the reporting insurance company.

### **Documentation Standards**

9. In order for an insurer-owned RMBS or CMBS to be eligible for the year-end modeling process, conducted pursuant to this section below, the analysis must be based on information, documentation and data of the utmost integrity. A Legacy Security must meet the Ongoing Information requirements. An RMBS, CMBS or Re-REMIC that is not a Legacy Security must meet the Initial Information and Ongoing Information requirements. For the purposes of determining a Re-REMIC's status as a Legacy Security, the closing date of the Re-REMIC (not the Underlying Security) shall be used. The SSG may, in its sole discretion, determine that the Initial Information and/or Ongoing Information is not sufficient and/or not reliable to permit the RMBS or CMBS CUSIP to be eligible for financial modeling. If the SSG determines that the Initial Information and/or Ongoing Information is not sufficient and/or not reliable to permit the RMBS or CMBS CUSIP to be eligible for financial modeling, it will communicate this decision to the insurer and invite a dialogue to ascertain whether alternative information is available that would be deemed sufficient and/or reliable by the SSG.

### **Initial Information Requirements**

10. An RMBS or CMBS meets the Initial Information Requirements if the security meets one of the following three conditions:
  - **RTAS** – The RMBS or CMBS was assigned a preliminary price grid or designation as described in this Part;
  - **Initial Sufficiency Filing** – The RMBS or CMBS was reviewed by SSG through an Initial Sufficiency Filing; or

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- **Safe Harbor** – The RMBS or CMBS meets the Safe Harbor requirements.

### Initial Sufficiency Information Filing

11. An insurance company may file Initial Sufficiency Information with the SSG for the purpose of obtaining a determination that an RMBS or CMBS CUSIP is eligible for financial modeling under the annual surveillance process discussed below. Initial Sufficiency Information is only filed once for any given RMBS or CMBS. Reporting insurance companies are solely responsible for providing the SSG with Initial Information. A determination by the SSG that a given RMBS or CMBS CUSIP is eligible for financial modeling after an Initial Sufficiency Filing assessment is subject to the further and continuing obligation that the SSG obtain or the insurer provide the SSG with updated Ongoing Information close to the date of the annual surveillance.
12. **Required Documents for Initial Sufficiency Filing** – An insurer that owns an RMBS or a CMBS for which Initial Information is not publicly available shall provide the SSG with the following documentation.
13. **RMBS** – Unless otherwise specified by the SSG in a Modeling Alert, as further described below, an Initial Filing for an RMBS consists of submission of Initial Information and Ongoing Information in the form of the following documentation:
  - Pooling and Servicing Agreement or similar
  - Prospectus, Offering Memorandum or similar; Accountant’s comfort letter
  - If applicable, ISDA Schedules and Confirmations or similar
  - Legal opinions given in connection with the transaction
  - Any other documents referenced by the above
  - Third-Party Due diligence scope document and raw results. If less than 100% due diligence, detailed description of the loan selection process
  - If applicable, loan purchase agreements or similar. Loan Tape
14. **CMBS** – Unless otherwise specified by the SSG in a Modeling Alert, as further described below, an Initial Filing for a CMBS consists of submission of Initial Information and Ongoing Information in the form of the following documentation:
  - Pooling and Servicing Agreement or similar
  - Prospectus, Offering Memorandum or similar; Accountant’s comfort letter
  - If applicable, ISDA Schedules and Confirmations or similar

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- Legal opinion given in connection with the transaction
- Any other documents referenced in the above
- Asset Summaries
- Loan Tape
- Loan documents, including reliable information about the terms of the transaction; including, but not limited to, financial covenants, events of default, legal remedies and other information about financial, contractual or legal aspects of the transaction in form and substance consistent with industry best practices for CMBS issuance.
- In certain cases, additional documents below will enable the SSG to verify and validate initial underwriting information of the property securing the CMBS. These documents may be required in form and substance consistent with best practices for typical CMBS issuance.
- Historical operating statements and borrower’s budget
- Underwriter’s analysis of stabilized cash flow with footnotes of assumptions used
- Property type specific, rent roll information
- Appraisals and other data from recognized industry market sources
- Independent engineering report (Property Condition Assessment)
- Environmental Site Assessment (ESA) – Phase I/Phase II
- Documentation related to seismic, flood and windstorm risks
- Franchise agreements and ground leases, if applicable
- Management agreements

### SSG Modeling Alerts

15. The SSG shall at all times have discretion to determine that differences in the structure, governing law, waterfall structure or any other aspect of a securitization or a class of securitization requires that insurance companies provide Initial Information and/or Ongoing Information additional to or different from that identified in this Part. The SSG shall communicate such additional or different documentation requirements to insurers by publishing a Modeling Alert on the NAIC website and scheduling a meeting of the VOS/TF to ensure public dissemination of the decision.

## Safe Harbor

16. Safe Harbor options serve as proxies for the Initial Sufficiency filing. The options reflect publicly available information that a third party has analyzed the Initial Information. Because the structured securities market is quite dynamic, the list of Safe Harbor options may change frequently, with notice and opportunity for comment, as described in this section. An RMBS or CMBS meets the Initial Information requirement if:

- At least two Section 17(g)-7 reports issued by different CRPs are publicly available; or
- A security that is publicly registered under the federal Securities Act of 1933.

## Ongoing Information Requirements

17. An RMBS or CMBS meets the Ongoing Information Requirements if Ongoing Information is available to the SSG and the relevant third-party vendor from an Original Source. The SSG, in its sole discretion and in consultation with the relevant third-party vendor, may determine that the Ongoing Information is not sufficient or reliable to permit a given RMBS or CMBS CUSIP to be financially modeled. However, in making such a determination, the SSG shall take into account reasonable market practices and standards.

## Special Rules for Certain Re-REMICs

18. Re-REMICs are generally simple restructurings of RMBS or CMBS. An Initial Sufficiency Filing for a Re-REMIC (a) which is not a Legacy Security itself but (b) where each Underlying Security is a Legacy Security shall not require submission of information regarding the Underlying Securities. In most cases, a prospectus for the Re-REMIC will be sufficient. If the SSG determines that additional information about the Re-REMIC structure or formation is required, it will communicate this decision to the insurer and invite a dialogue to ascertain whether additional information is available that would be deemed sufficient by the SSG.



## ANALYTICAL ASSIGNMENTS

### ANNUAL SURVEILLANCE OF RMBS AND CMBS – MODELED AND NON-MODELED SECURITIES

#### Scope

19. This section explains the financial modeling methodology applicable to **all** RMBS and CMBS (defined above) securitizations, ~~and~~ the book/adjusted carrying value methodology applicable to **a modeled Legacy Security, the NAIC Designation Intrinsic Price Mapping applicable to a modeled non-Legacy Security,** and non-modeled securities subject to *SSAP No. 43R—Loan-Backed and Structured Securities*. Please refer to SSAP No. 43R for a description of securities subject to its provisions. The VOS/TF does not formulate policy or administrative procedures for statutory accounting guidance. Reporting insurance companies are responsible for determining whether a security is subject to SSAP No. 43R and applying the appropriate guidance.

#### Important Limitation on the Definitions of RMBS and CMBS

20. The definitions of RMBS and CMBS above are intended solely to permit the SSG to communicate with financial modeling vendors, insurance company investors who own RMBS and CMBS subject to financial modeling and/or the book/adjusted carrying value methodology and their investment advisors to facilitate the performance by the SSG of the financial modeling methodology described below. The definitions contained in this section are not intended for use and should not be used as accounting or statutory statement reporting instructions or guidance.

**NOTE:** Please refer to *SSAP No. 43R—Loan-Backed and Structured Securities* for applicable accounting guidance and reporting instructions.

### ANALYTICAL PROCEDURES APPLICABLE TO RMBS AND CMBS SECURITIZATIONS SUBJECT TO FINANCIAL MODELING METHODOLOGY

#### Filing Exemption Status of RMBS and CMBS

21. RMBS and CMBS are not eligible for ~~the~~ filing exemption because credit ratings of CRPs are no longer used to set risk-based capital (RBC) for RMBS or CMBS. However, RMBS and CMBS are not submitted to the SSG.

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## Use of Financial Modeling for Year-End Reporting for RMBS and CMBS

22. Beginning with year-end 2009 for RMBS and 2010 for CMBS, probability weighted net present values will be produced under NAIC staff supervision by an NAIC-selected vendor using its financial model with defined analytical inputs selected by the SSG. The vendor will provide the SSG with a **Intrinsic Price and/or a range of net present values** for each RMBS or CMBS corresponding to each NAIC Designation category. The NAIC Designation for a specific **Legacy Security** RMBS or CMBS is determined by the insurance company, based on book/adjusted carrying value ranges, **and the NAIC Designation for a specific non-Legacy Security RMBS or CMBS is determined by the NAIC Designation Intrinsic Price Mapping by SSG.**

**NOTE:** Please refer to *SSAP No. 43R—Loan-Backed and Structured Securities* for guidance on all accounting and related reporting issues.

## Analytical Procedures for RMBS and CMBS

23. The SSG shall develop and implement all necessary processes to coordinate the engagement by the NAIC of a vendor who will perform loan-level analysis of insurer-owned RMBS and CMBS using the vendor's proprietary models.

<b>RMBS AND CMBS SUBJECT TO FINANCIAL MODELING</b>
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## Setting Microeconomic Assumptions and Stress Scenarios

24. Not later than September of each year, the SSG shall begin working with the vendor to identify the assumptions, stress scenarios and probabilities (hereafter model criteria) the SSG intends to use at year-end to run the vendor's financial model.

## The Financial Modeling Process

25. Information about the financial modeling process can be found at [www.naic.org/structured\\_securities/index\\_structured\\_securities.htm](http://www.naic.org/structured_securities/index_structured_securities.htm).

**Use of Net Present Value and Carrying Value for Financially Modeled Legacy Security RMBS and CMBS**

26. For each modeled Legacy Security RMBS and CMBS, the financial model determines the net present value at which the expected loss equals the midpoint between the RBC charges for each NAIC Designation; i.e., each price point, if exceeded, changes the NAIC Designation. Net present value is the net present value of principal losses, discounted using the security’s coupon rate (adjusted in case of original issue discount securities to book yield at original issue and in case of floating rate securities, discounted using LIBOR curve + Origination spread). Because of the difference in RBC charge, the deliverable is five values for each RMBS and CMBS security for companies required to maintain an asset valuation reserve (AVR) and five values for companies not required to maintain an AVR. This is illustrated in the chart below.

**RBC charge / NAIC designation (pre-tax)**

P&C	RBC	Midpoint
1	0.3%	0.65%
2	1.0%	1.50%
3	2.0%	3.25%
4	4.5%	7.25%
5	10.0%	20.00%
6	30.0%	
Life	RBC	Midpoint
1	0.4%	0.85%
2	1.3%	2.95%
3	4.6%	7.30%
4	10.0%	16.50%
5	23.0%	26.50%
6	30.0%	

27. The NAIC Designation and NAIC Designation Category for a given modeled **Legacy Security** RMBS or CMBS CUSIP owned by a given insurance company depends on the insurer’s book/adjusted carrying value of each RMBS or CMBS, whether that carrying value, in accordance with *SSAP No. 43R—Loan-Backed and Structured Securities*, paragraphs 25 through 26a, is the amortized cost or fair value, and where the book/adjusted carrying value matches the price ranges provided in the model output for each NAIC Designation and the mapped NAIC Designation Category, reflected in the table below, to be used for reporting an NAIC Designation Category until new Risk Based Capital factors are adopted for each NAIC Designation Category and new prices ranges developed; ~~except that an RMBS or CMBS tranche that has no expected loss under any of the selected modeling scenarios and that would be equivalent to an NAIC 1 Designation if the filing exempt process were used, would be assigned an NAIC 1 Designation and NAIC 1.D Designation Category~~ regardless of the insurer’s book/adjusted carrying value.

**NOTE:** Please refer to the detailed instructions provided in SSAP No. 43R.

NAIC Designation Determined by Modeled Price Ranges	Mapped NAIC Designation Category
1	1.D
2	2.B
3	3.B
4	4.B
5	5.B
6	6

**Use of Intrinsic Price for Financially Modeled non-Legacy Security RMBS and CMBS**

28. The NAIC Designation and NAIC Designation Category for a given modeled non-Legacy Security RMBS or CMBS CUSIP owned by a given insurance is assigned by SSG and **does not** depend on the insurer’s book/adjusted carrying value of each RMBS or CMBS. The NAIC Designation and Designation Category assigned will be determined by applying the Intrinsic Price to the NAIC Designation Intrinsic Price Mapping, as defined in this Part.

**SECURITIES NOT MODELED BY THE SSG AND NOT RATED BY AN NAIC CRP  
OR DESIGNATED BY THE SVO**

29. Securities subject to *SSAP No. 43R—Loan-Backed and Structured Securities* that cannot be modeled by the SSG and are not rated by an NAIC CRP or designated by the SVO are either: (a) assigned the NAIC administrative symbol **ND** (not designated), requiring subsequent filing with the SVO; or (b) assigned the NAIC Designation for Special Reporting Instruction [i.e., an **NAIC 5GI**, NAIC Designation Category **NAIC 5.B GI** or **NAIC 6\*** (six-star)].

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## **MORTGAGE REFERENCED SECURITIES**

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### **Definition**

30. A Mortgage Referenced Security has the following characteristics: A Mortgage Referenced Security's coupon and/or principal payments are linked, in whole or in part, to prices of, or payment streams from, real estate, index or indices related to real estate, or assets deriving their value from instruments related to real estate, including, but not limited to, mortgage loans.

### **Not Filing Exempt**

31. A Mortgage Referenced Security is not eligible for filing exemption but is subject to the filing requirement.

### **NAIC Risk Assessment**

32. In determining the NAIC Designation of a Mortgage Referenced Security, the SSG may use the financial modeling methodology discussed in this Part, adjusted (if and as necessary) to the specific reporting and accounting requirements applicable to Mortgage Referenced Securities.

### **Quarterly Reporting for Mortgage Reference Securities**

33. To determine the NAIC Designation to be used for quarterly financial statement reporting for a Mortgage Reference Security purchased subsequent to the annual surveillance described in this Part, the insurer uses the prior year-end modeling data for that CUSIP (which can be obtained from the NAIC) until the annual surveillance data is published for the current year. For a Mortgage Reference Security that is not in the prior year-end modeling data for that CUSIP, the insurer may follow the instructions in Part Two of this manual for the assignment of the SVO Administrative Symbol "Z" provided the insurer owned security meets the criteria for a security that is in transition in reporting or filing status.

**NOTE:** Please refer to SSAP No. 26R and SSAP No. 43R for the definition of and guidance on Structured Notes and Mortgage Referenced Securities. Please also refer to Part Three of this Manual for guidance about the filing exempt status of Structured Notes.

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## **GROUND LEASE FINANCING TRANSACTIONS**

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### **Definition**

34. Ground Lease Financing (GLF) transactions are defined and explained in “Ground Lease Financing Transactions” in Part Three of this Manual.

### **SSG Role and Process**

1. On occasion, the SVO may refer a GLF transaction to the SVO for financial modeling of the GLF space leases or business operation, as applicable, in accordance with the process set forth in “Ground Lease Financing Transactions” in Part Three of this Manual. Following an SVO referral the SSG and SVO will maintain open communication related to requests for additional data, analytical questions and analytical conclusions. Any GLF transaction NAIC Designation will be assigned by the SVO.

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## THE RTAS – EMERGING INVESTMENT VEHICLE

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### Purpose

2. Price grids **and/or Designations and Designation Categories** are generated for the exclusive use of insurance companies and the NAIC regulatory community. Insurance companies use official Price Grids **and/or Designations and Designation Categories** by following the instructions in *SSAP No. 43R—Loan-Backed and Structured Securities* to derive a final NAIC Designation for the RMBS or CMBS, which they use to derive the RBC applicable for the RMBS or CMBS.

**NOTE:** Please refer to SSAP No. 43R for a full explanation of the applicable procedure.

### Extension of Authority

3. The Regulatory Treatment Assessment Service – Emerging Investment Vehicle procedure is extended to the SSG, and the SSG is authorized to determine probable regulatory treatment for RMBS and CMBS pursuant to this Part or for other securities, where, in the opinion of the SSG, financial modeling methodology would yield the necessary analytical insight to determine probable regulatory treatment or otherwise enable the SSG to make recommendations to the VOS/TF as to regulatory treatment for a security.

### Interpretation

4. To facilitate this purpose, wherever in the Regulatory Treatment Assessment Service – Emerging Investment Vehicle procedure reference is made to the SVO, it shall be read to also refer to and apply to the SSG, adjusting for differences in the operational or methodological context. The Regulatory Treatment Assessment Service – Emerging Investment Vehicle procedure shall also be read as authority for collaboration between SVO and SSG staff functions so as to encompass RTAS assignments that require the use of SVO financial, corporate, municipal, legal, and structural analysis and related methodologies, as well as of financial modeling methodologies.



## Translation of Preliminary into Official Price Grids and/or NAIC Designations and Designation Categories

5. Price Grids and/or Designations and Designation Categories (“PGD”) generated by the SSG pursuant to an RTAS are preliminary within the meaning of that term as used in the Regulatory Treatment Assessment Service – Emerging Investment Vehicle procedure and accordingly cannot be used for official NAIC regulatory purposes. Preliminary NAIC Designations are translated into official NAIC Designations by the SVO when an insurance company purchases and files the security and the SVO conducts an official assessment. However, this Manual does not require the filing of RMBS and CMBS subject to financial modeling methodology with the SSG. It is, therefore, necessary to specify a procedure for the translation of preliminary Price Grids and/or Designations and Designation Categories (“Preliminary PGD”) into official ~~Price Grids~~-PGD that can be used for NAIC regulatory purposes. Preliminary ~~Price Grids~~-PGDs generated by the SSG become an official ~~Price Grid~~ PGD within the meaning of this section when an insurance company has purchased the security for which the ~~Price Grid~~ PGD was generated and reported that security for quarterly reporting purposes using the SSG generated ~~Price Grid~~ PGD. A ~~Price Grid~~ PGD for a security reported by an insurance company for quarterly reporting is effective until the SSG conducts the next annual surveillance pursuant to this Part at which the time the ~~Price Grid~~ PGDs generated by the SSG at year-end shall be the official ~~Price Grid~~ PGDs for that security.

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MEMORANDUM

TO: Kevin Fry, Chair, Valuation of Securities (E) Task Force  
Members of the Valuation of Securities (E) Task Force

FROM: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)  
Marc Perlman, Investment Counsel, NAIC Securities Valuation Office (SVO)

CC: Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

RE: **Updated** - Proposed Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) to Private Rating Letter Rationale Report Only

DATE: **December 7, 2020** ~~October 30, 2020~~

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**1. Summary** –The IAO staff discussed with the Task Force at its May 14<sup>th</sup> meeting the IAO’s concerns with bespoke securities and the NAIC’s excessive reliance on credit rating provider (CRP) ratings to assess investment risk and for regulatory purposes. At that meeting the Task Force exposed the IAO’s memorandum, dated February 27, 2020, summarizing these concerns. The Task Force requested the SVO make incremental recommendations to address these issues.

On October 23<sup>rd</sup> of this year the Financial Condition (E) Committee directed the Task Force to include a new charge for 2021; specifically, to, “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.” In furtherance of the proposed new Task Force charge and the Task Force’s request for incremental recommendations, the SVO proposes taking a first step towards implementation of some of its recommendations in its memo by increasing SVO scrutiny of PL securities, many of which are bespoke securities.

At the Task Force meeting on November 14<sup>th</sup>, the Task Force directed the SVO to update its proposed amendment to have the Private Rating Letter Rationale Reports filed with the SVO but without the SVO’s discretion over evaluating the appropriateness of the rating or methodology utilized, at least at this time. The SVO still recommends that it be granted this oversight authority and will be scheduling a regulator-only call in 2021 to review with the Task Force PLR transactions which appear to be either ineligible for filing exemption, ineligible for Schedule D reporting and/or where there is a material difference in opinion as to the risk

**2. Recommendation for oversight of PL Securities** – In its bespoke securities memo the SVO described its concern that its lack of authority to use its judgment in determining whether a CRP rating is useful for NAIC purposes (meaning its rating methodology may not be appropriate for, or consistent with, the assessment of investment risk for statutory purposes) has fed an increase in the use of bespoke securities, many of which are assigned NAIC designations through the Filing Exempt (FE) process, which includes the private letter rating process. To begin to address this lack of meaningful oversight of CRP ratings, the SVO proposes, as it did in its memo, that securities assigned private letter ratings be submitted to it for review. Understanding the many CRP private rating letters include little or no analysis

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beyond the assigned private rating, the SVO recommends that for a PL security to receive an NAIC Designation the SVO must receive, along with the private rating letter, a related private rating letter rationale report providing more in-depth analysis of the transaction, the methodology used to arrive at the private rating, and, as appropriate, discussion of the transaction's credit, legal and operational risks and mitigants. With both the private rating letter and the private rating letter rationale report the SVO would be able to determine (i) whether the private credit rating is an Eligible NAIC CRP Rating, meaning the security type is eligible to be reported on Schedule D and that it is appropriate for and NRSRO credit rating to be used to determine the regulatory treatment of the security, and (ii) whether the SVO agrees with the private credit rating. The SVO would have full discretion, based on its reasonable review of the private rating letter and the supporting rationale report, to assign an NAIC designation equivalent to the CRP PLR, to require the security to be filed for review or, to decline to assign any NAIC designation.

The SVO understands there are potential obstacles to attaining private rating letter rationale reports such as CRP confidentiality policies. However, the SVO thinks such analysis is crucial to its ability to best determine whether a rating is a satisfactory assessment of investment risk for statutory purposes due to the typical private rating letter's lack of analysis and transparency. As such the SVO is committed to working with industry and CRPs to find solutions to possible obstacles.

**3. Proposed Amendment** – The SVO proposes the following amendments to Parts One and Three of the Purposes and Procedures Manual of the Investment Analysis Office to permit the SVO to review all PL securities whether processed through a feed or submitted directly to the SVO and would require insurance company filers to provide private rating letter rationale reports for each security. The following text in red shows the proposed Purposes and Procedures Manual revisions. Updates are highlighted in yellow.

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**PART ONE**  
**POLICIES OF THE NAIC VALUATION OF SECURITIES (E) TASK FORCE**

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**FILING EXEMPTIONS**

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<p><b>POLICIES APPLICABLE TO FILING EXEMPT (FE) SECURITIES AND PRIVATE LETTER (PL) RATING SECURITIES</b></p>
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**Policy Considerations**

83. In connection with the implementation of the verification procedure for PL securities, the VOS/TF acknowledges that the practices adopted by NAIC CRPs in relation to the distribution of private rating letters for what the NAIC refers to as PL securities, including their confidentiality procedures and agreements, are integral to the business models of private for-profit entities that the NAIC does not regulate and which the NAIC stands in the relation of a customer of rating services. Accordingly, the SVO, as NAIC staff, shall not be responsible for negotiating with NAIC CRPs to modify their confidentiality practices or provide data-feeds to the SVO. However, if an NAIC CRP shall determine that it is willing to modify its confidentiality provisions or provide such data-feed or an alternative process so that the SVO can obtain electronically, copies of private rating letters and private rating letter rationale reports for PL securities issued by that NAIC CRP instead of by requiring insurers to provide PDF files, then the SVO is authorized to work with the NAIC CRP to obtain and integrate the private rating letters and private rating letter rationale reports or the data-feeds into NAIC systems to create electronic processes that will permit electronic verification that the insurer-owned PL security have been assigned an NAIC CRP Eligible Credit Rating. Individual insurers and/or representatives of the insurance industry are encouraged to find ways to resolve confidentiality restrictions imposed by NAIC CRPs on the private rating letter and private rating letter rationale report or to influence the process as investors to encourage NAIC CRPs to provide the data-feeds to the SVO or alternative methods to permit the SVO to obtain NAIC CRP credit ratings and private rating letter rationale report for PL securities to be used to administer the PL securities verification procedure specified in this section.



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**PART THREE**  
**SVO PROCEDURES AND METHODOLOGY FOR PRODUCTION**  
**OF NAIC DESIGNATIONS**

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**PROCEDURE APPLICABLE TO FILING EXEMPT (FE) SECURITIES AND PRIVATE LETTER (PL)  
RATING SECURITIES**

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<b>PL SECURITIES</b>
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**Effective Date of Verification Procedure for PL Securities**

9. Effective January 1, 2022, for each PL security received by the SVO either through a copy of a private rating letter or in a CRP credit rating feed, insurance companies shall be responsible for providing the SVO a copy of the related private rating letter rationale report from the applicable NAIC CRP, until such time as industry representatives and the SVO shall have established reliable procedures for obtaining the necessary information on credit ratings directly from the NAIC CRPs.
10. Effective July 1, 2018, insurance companies shall be responsible for providing the SVO copies of private rating letters for PL securities, where applicable, until such time as industry representatives and the SVO shall have established reliable procedures for obtaining the necessary information on credit ratings directly from the NAIC CRPs.
11. For **PL** Securities issued prior to January 1, 2018, if an insurance company cannot provide a copy of the rating letter to the SVO due to confidentiality concerns and the rating is not included in a CRP credit rating feed (or other form of direct delivery from the NAIC CRP), the insurer shall report such securities on such securities' General Interrogatory to be developed for this purpose (i.e., a **PL GI** security).

**Definitions**

12. For purposes of this section:
  - The phrase “private rating letter” means a letter or report issued by an NAIC CRP on its letterhead or its controlled website to an issuer or investor, obtained by an insurer in its capacity as an investor in the issuance or by following the confidentiality process established by the NAIC CRP.
  - The phrase “privately rated security” means a security issued by an issuer wherein the issuer has solicited a credit rating for the issuance from an NAIC CRP and the NAIC CRP has agreed to issue a credit rating for the issuance to be communicated to the issuer and a specified group of investors only and not publicly released via the NAIC CRP’s public data feed or website. The privately rated security is the subject of the private rating letter and is referred to herein as a private letter (PL) security.

- The phrase “private rating letter rationale report” means an analytical review of the privately rated security explaining the transaction structure, methodology relied upon, and, as appropriate, analysis of the credit, legal and operational risks and mitigants supporting the assigned NAIC CRP rating, in a report issued by an NAIC CRP on its letterhead or its controlled website to an issuer or investor, obtained by an insurer in its capacity as an investor in the issuance or by following the confidentiality process established by the NAIC CRP.

### Conditions to Filing Exemption for PL Securities Issued on or After January 1, 2018

13. **PL** securities are exempt from filing with the SVO for assignment of an analytically determined NAIC Designation if the security has been assigned an Eligible NAIC CRP Credit Rating, ~~and~~ the insurer verifies the rated status of the **PL** security to the SVO, ~~the insurer or NAIC CRP provides the SVO with the private rating letter rationale report, and the SVO concurs with the assigned Eligible NAIC CRP Credit Rating and the SVO deems the privately rated security eligible to receive an NAIC Designation with an NAIC CRP Credit Rating.~~
14. If the **PL** security is not rated by an NAIC CRP; or a credit rating is assigned that is not an Eligible NAIC CRP Credit Rating; or if the insurer cannot provide the SVO a private rating letter verifying that the assigned credit rating is an Eligible NAIC CRP Credit Rating; or the NAIC CRP cannot provide the Eligible NAIC CRP Credit Rating on the **PL** security to the NAIC through an electronic data feed approved by the SVO and that specifically identifies the **PL** securities rated by that NAIC CRP; ~~or the insurer or NAIC CRP cannot provide the private rating letter rationale report; or the SVO does not concur with the assigned Eligible NAIC CRP Credit Rating based on its review of the private letter rating rationale report;~~ or the SVO deems the privately rated security ineligible to receive an NAIC Designation with a NAIC CRP Credit Rating, the **PL** security is not filing exempt.
15. An insurer that owns a **PL** security that is not filing exempt shall either: (a) file the security with the necessary documentation with the SVO for an analytically determined NAIC Designation; or (b) self-assign an **NAIC 5GI** to the security and report using the Interrogatory procedure; in either case within 120 days of purchase.



### Conditions to Filing Exemption for PL Securities Issued Prior to January 1, 2018

16. **PL** securities issued prior to January 1, 2018 are exempt from filing with the SVO for assignment of an analytically determined NAIC Designation if the security has been assigned an Eligible NAIC CRP Credit Rating. If the **PL** security CRP rating is not included in the applicable CRP credit rating feed (or other form of direct delivery from the CRP) or the insurer cannot submit the private letter rating to the SVO because of confidentiality provisions, the security shall be designated **PLGI**. Insurers shall report on all such securities in a General Interrogatory with an attestation that all such securities have an Eligible CRP Credit and are reflected in the financial statements and risk-based capital calculation commensurate with that rating

### Procedure

17. The NAIC shall create systems and develop and staff administrative and operational procedures to be administered by the SVO to identify insurer-owned **PL** securities; verify whether or not the assigned credit rating is an Eligible NAIC CRP Credit Rating, review the private rating letter rationale report, and either translate that credit rating into its equivalent NAIC Designation and input the NAIC Designation for the security into the appropriate NAIC systems or notify the insurer that the security is not eligible for filing exemption.

### SVO to Administer Verification Procedures

18. It shall be the responsibility of the NAIC to create and maintain for the SVO, electronic facilities to accept: (a) electronic data-feeds provided by NAIC CRPs containing and specifically identifying the **PL** securities rated by that NAIC CRP, ~~and~~ the credit rating assigned to the **PL** securities and the supporting private rating letter rationale report; or (b) PDF files of private rating letters provided by insurers to the SVO containing the NAIC CRP credit rating for the **PL** security and a copy of the supporting private rating letter rationale report.

### The PL Process

19. It shall be the responsibility of the SVO to identify **PL** securities in the AVS+ system for insurance companies to use when reporting **PL** securities to the NAIC as part of the NAIC's Financial Statement Blank reporting process. The SVO identifies **PL** securities when it conducts the quarterly compilation of the SVO List of Securities.

### Producing NAIC Designations for PL Securities

20. The SVO shall produce NAIC Designations for securities subject to private letter ratings as follows:

- The insurance company shall file a copy of the private rating letter with the SVO if not included in the applicable NAIC CRP Rating feed(s) (or other form of direct delivery from the CRP) noted above in Conditions to Filing Exemption for PL Securities and **the supporting private rating letter rationale report, if the SVO has not received it directly from the CRP, within the initial filing deadline for newly acquired securities or securities in transition (as explained in “SVO Analytical Department Symbols” in Part Two of this Manual) and each calendar year thereafter along with any changes in PL Securities rating.** In instances where the **PL** security is included in the applicable NAIC CRP Rating feed(s), the SVO shall follow the procedure for Filing Exempt (FE) securities **only after the SVO receives both the private rating letter and private rating letter rationale report either directly or through a NAIC CRP Rating feed(s), and if, in its sole discretion, it concurs with the assigned Eligible NAIC CRP Credit Rating after reviewing the private rating letter rationale report and the SVO** deems the privately rated security eligible to receive an NAIC Designation with an NAIC CRP Credit Rating.
- In instances where a private letter **and private rating letter rationale report** is filed, the SVO shall evaluate the private letter **and private rating letter rationale report** to determine whether the security has been assigned an Eligible NAIC CRP Rating **and if the privately rated security is eligible to receive an NAIC Designation with a NAIC CRP Credit Rating.** Similar to public securities where a rating is received directly from the CRP via electronic feeds, **there is a similar assumption for the PL security,** that the **rating** meets the definition of an Eligible NAIC CRP Rating as a normal part of the CRP rating process, absent evidence to the contrary in the rating letter **or private rating letter rationale report** (e.g., evidence that the rating applies only to principal or interest, in a deviation from the normal CRP rating process).
- If the SVO verifies that the security has been assigned an Eligible NAIC CRP Rating and **if the SVO, upon review of the private rating letter rationale report and in its sole discretion, concurs with the assigned Eligible NAIC CRP Credit Rating** deems the privately rated security eligible to receive an NAIC Designation with a **NAIC CRP Credit Rating,** it assigns an NAIC Designation in accordance with the policy and procedure specified in this Manual. The assumption in the application of this step of the procedure is that **PL** securities are typically assigned a credit rating by only one NAIC CRP. However, if this assumption is inaccurate for any **PL** security, the SVO applies the same procedure specified for FE securities.

21. If the SVO verifies that the security:

- Has been assigned a credit rating but that the credit rating is not an Eligible NAIC CRP Credit Rating; or
- Has not been rated by an NAIC CRP; or

- Is no longer subject to a private letter rating; or
- ~~Has an assigned Eligible NAIC CRP Credit Rating that the SVO, in its sole discretion, does not concur with; or~~
- Is a type of security that is ineligible to receive an NAIC Designation with a NAIC CRP Credit Rating

The SVO shall notify the insurer that the security is not eligible for filing exemption. The insurance company shall then either file that security and necessary documentation with the SVO for an independent credit assessment or assign an **NAIC 5GI** Regulatory Designation to the security in the related Interrogatory.

22. An **NAIC 5GI** Designation may also be used in connection with the designation of **PL** securities rated by an NAIC CRP (i.e., for private letter ratings issued on or after January 1, 2018) when the documentation is not available for the SVO to assign an NAIC Designation. For purposes of this section, the documentation is not available for the SVO to assign an NAIC Designation if the NAIC CRP credit rating is not included in the applicable CRP credit rating feed (or other form of direct delivery from the NAIC CRP) and the insurer is unable to provide a copy of the private letter rating documentation, **including the private rating letter rationale report**, necessary for the SVO to assign an NAIC Designation.

G:\SECVAl\DATA\Vos-tf\Meetings\2021\February\VOSTF 02-18-2021\02 - Require Filing Private Rating Analysis\2020-023.02 PP Manual Amend - Updated Private Rating Rationale Analysis v5.docx



February 5, 2021

Mr. Kevin Fry, Chair  
 Ms. Carrie Mears, Vice Chair  
 NAIC Valuation of Securities Task Force  
 1100 Walnut Street  
 Suite 1500  
 Kansas City, MO 64106-2197

Re: Updated – Proposed Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual) to Private Rating Letter Rationale Report Only

Dear Mr. Fry and Ms. Mears:

The American Council of Life Insurers (“ACLI”)<sup>1</sup>, Private Placement *investors* Association (“PPiA”)<sup>2</sup>, and the North American Securities Valuation Association (“NASVA”)<sup>3</sup>, (collectively, “the undersigned”) would like to thank the Valuation of Securities Task Force (“VOSTF”) for the opportunity to comment on the exposed proposed amendments to the P&P Manual related to the filing of Private Rating Letter

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<sup>1</sup> The **American Council of Life Insurers** (ACLI) is the leading trade association driving public policy and advocacy on behalf of the life insurance industry. 90 million American families rely on the life insurance industry for financial protection and retirement security. ACLI’s member companies are dedicated to protecting consumers’ financial wellbeing through life insurance, annuities, retirement plans, long-term care insurance, disability income insurance, reinsurance, and dental, vision and other supplemental benefits. ACLI’s 280 member companies represent 94 percent of industry assets in the United States.

<sup>2</sup> The **Private Placement Investors Association** (PPiA) is a business association of insurance companies, other institutional investors, and affiliates thereof, that are active investors in the primary market for privately placed debt instruments. The association exists to provide a discussion forum for private debt investors; to facilitate the development of industry best practices; to promote interest in the primary market for privately placed debt instruments; and to increase accessibility to capital for issuers of privately placed debt instruments. The PPiA serves 63 member companies and works with regulators, NASVA, the American College of Investors Counsel, and the investment banking community to efficiently implement changes within the private placement marketplace. Learn more at [www.usppia.com](http://www.usppia.com).

<sup>3</sup> The **North American Securities Valuation Association** (NASVA) is an association of insurance company representatives who interact with the National Association of Insurance Commissioners Securities Valuation Office to provide important input, and to exchange information, in order to improve the interaction between the SVO and its users. In the past, NASVA committees have worked on issues such as improving filing procedures, suggesting enhancements to the NAIC’s ISIS electronic security filing system, and commenting on year-end processes. Find more information [here](#)

Rationale Reports. We remain committed to assisting the VOSTF in addressing regulatory concerns surrounding bespoke securities, which are often (but not always) found in the private letter rating space.

As previously shared with the NAIC, an April 2019 study, "Society of Actuaries; 2003-2015 Credit Loss Experience Study: Private Placement Bonds" demonstrated the superior track record of private placement bonds compared to public bonds. Specifically, data from the study showed that private placement bonds had lower economic loss rates (which translates to superior performance) than public bonds during the period of the study. Additionally, private placement bonds offer several advantages to investors over public bonds, including the opportunity to negotiate more advantageous terms, additional covenants / credit protection for the investor, call premiums, and additional compensation for illiquidity. This asset class has become essential to insurance companies during this low yield environment, providing a significant source of income and duration to insurance company portfolios. Given this, the undersigned greatly appreciate VOSTF's recognition that capital uncertainty in the private placement market would pressure insurance companies to reduce allocations to this asset class as well as pressure both issuers and investment bankers to steer such investments away from the insurance market.

The undersigned also appreciate the VOSTF's decision to gather additional information on insurer's privately rated securities before making policy decisions regarding the future regulation of these securities. We generally agree that the proposed changes to the P&P Manual will enhance transparency and the Securities Valuation Office's (SVO) ability to be the eyes and ears of the VOSTF. However, as a friendly amendment, the undersigned offer some proposed amendments (tracked and highlighted in green) that we believe provide necessary clarification in the P&P Manual as to the reasons for which the SVO may deem a privately rated security ineligible to receive an NAIC Designation with a NAIC Credit Rating Provider (CRP) Rating.

### **Legal and Operational Considerations**

As outlined in our letter in response to the Issue Paper "IAO staff concerns about Bespoke Securities, and Reliance on CRP Ratings", the undersigned proposed a solution to increase the level of transparency and information sharing with the SVO, and by extension regulators, to address potential concerns with Bespoke Securities by sharing private rating letters, and rating rationale reports (where available), and if necessary, deal documents (upon the SVO's request). This would allow the SVO to identify specific problems so they can be addressed in a public and transparent way and be responsive to the Financial Condition (E) Committee's charge.

In that letter, the undersigned also raised the practical challenges resulting from the contractual agreements between NAIC CRPs, investors and issuers regarding the nature of the rating services provided. These agreements contain confidentiality provisions as well as terms related to the level of disclosure and analysis that will be provided initially, and on a going forward basis. Previously, industry worked diligently with rating agencies and issuers to amend confidentiality provisions allowing private rating letters to be filed with the SVO and allowing the private ratings to flow through to the SVO on electronic feeds, but for some NAIC CRPs, that did not include the right for insurers to also share ratings rationale reports with the SVO.

Given this, and while the undersigned are clearly supportive of increasing the level of transparency, we request that the VOSTF and the SVO consider the following practical considerations:

- 1) *Timing*: Requiring that insurers provide, for all privately rated securities issued from 1/1/18 thru 1/1/22, rating rationales as well as ratings letters, will in many instances conflict with the agreed upon work product in the contractual agreements between the issuers and the NAIC CRPs. These contracts may also contain limitations on how ratings and any related rationales can be shared. Hence, the undersigned propose that for securities issued in the period from and after 1/1/18 and prior to 1/1/22, the requirement to furnish rating rationales be on a best-efforts basis. This requirement would apply without qualification for securities issued on or after 1/1/22. This avoids the massive disruption that would occur if, for a great many securities issued in the four years commencing 1/1/18, insurers would need to persuade issuers and NAIC CRPs to amend existing contractual arrangements, with no certainty that such efforts would be successful. Further, we note that the SAPWG's SSAP No. 43R Project (or Schedule D Project) will be addressing the scope of Schedule D Bonds and alleviate a significant concern related to Bespoke Securities. Such a friendly amendment is included in Paragraphs 11 and 22 (tracked and highlighted in blue).
- 2) *Ongoing versus initial reports*: The undersigned would also like to clarify that the expectation to provide fulsome ratings rationales only applies upon the initial issuance by a NAIC CRP of a security specific rating. The initial issuance of an NAIC CRP rating usually occurs in connection with a newly issued security, but it may also occur after the fact, for a security that was initially unrated, or when an additional or different NAIC CRP starts to issue ratings specific to the same security. Once a ratings rationale by the applicable NAIC CRP has been furnished, subsequent changes by the NAIC CRP to the rating for the relevant security may be made by ratings letters only without any requirement for rationale reports as well. This is reflective of a very common commercially negotiated point between the issuer and the NAIC CRP, as it lowers the ongoing cost for the issuers that may otherwise seek to issue debt in a competing market.
- 3) *Rating rationale reports*: In our discussions with NAICCRPs, some have expressed a desire to better understand what type of work product is expected in a rating rationale report (e.g. how in depth the report should be, and what are the key topics that should be covered?). To help minimize any expectation gap with regards to rating rationale reports among rating agencies, insurers, issuers and the SVO, specifically on the level of detail and information most beneficial to the SVO (as broadly outlined in paragraph 12), we stand ready to continue working with the rating agencies and SVO to ensure this process goes as smoothly as possible.

As it pertains to the above considerations, industry commits to work in good faith with the issuers, investment bankers, and NAIC CRPs to take the necessary actions that will allow for the sharing of ratings rationales going forward. We do, however, expect this process to take time. As we work towards adopting this change, we will ensure the SVO is continually aware of our progress towards our shared goal of increased transparency and information sharing.

\* \* \*

We look forward to continued dialogue with the Members and staff on this critical issue. Do not hesitate to contact us if you require any clarity or have questions on this submission.

Sincerely,



Mike Monahan  
American Council of Life Insurer

*Tracey Lindsey*

Tracey Lindsey  
NASVA

*John Petchler*

John Petchler  
on behalf of PPIA Board of Directors

cc: Charles Therriault, Director, Securities Valuation Office



## MEMORANDUM

TO: Kevin Fry, Chair, Valuation of Securities (E) Task Force  
Members of the Valuation of Securities (E) Task Force

FROM: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)  
Marc Perlman, Investment Counsel, NAIC Securities Valuation Office (SVO)

CC: Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

RE: **Updated** - Proposed Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) to Private Rating Letter Rationale Report Only

DATE: **December 7, 2020** ~~October 30, 2020~~

**1. Summary** –The IAO staff discussed with the Task Force at its May 14<sup>th</sup> meeting the IAO’s concerns with bespoke securities and the NAIC’s excessive reliance on credit rating provider (CRP) ratings to assess investment risk and for regulatory purposes. At that meeting the Task Force exposed the IAO’s memorandum, dated February 27, 2020, summarizing these concerns. The Task Force requested the SVO make incremental recommendations to address these issues.

On October 23<sup>rd</sup> of this year the Financial Condition (E) Committee directed the Task Force to include a new charge for 2021; specifically, to, “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.” In furtherance of the proposed new Task Force charge and the Task Force’s request for incremental recommendations, the SVO proposes taking a first step towards implementation of some of its recommendations in its memo by increasing SVO scrutiny of PL securities, many of which are bespoke securities.

At the Task Force meeting on November 14<sup>th</sup>, the Task Force directed the SVO to update its proposed amendment to have the Private Rating Letter Rationale Reports filed with the SVO but without the SVO’s discretion over evaluating the appropriateness of the rating or methodology utilized, at least at this time. The SVO still recommends that it be granted this oversight authority and will be scheduling a regulator-only call in 2021 to review with the Task Force PLR transactions which appear to be either ineligible for filing exemption, ineligible for Schedule D reporting and/or where there is a material difference in opinion as to the risk

**2. Recommendation for oversight of PL Securities** – In its bespoke securities memo the SVO described its concern that its lack of authority to use its judgment in determining whether a CRP rating is useful for NAIC purposes (meaning its rating methodology may not be appropriate for, or consistent with, the assessment of investment risk for statutory purposes) has led to an increase in the use of bespoke securities, many of which are assigned NAIC designations through the Filing Exempt (FE) process, which includes the private letter rating process. To begin to address this lack of meaningful oversight of CRP ratings, the SVO proposes, as it did in its memo, that securities assigned private letter ratings be submitted to it for review. Understanding the many CRP private rating letters include little or no analysis

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beyond the assigned private rating, the SVO recommends that for a PL security to receive an NAIC Designation the SVO must receive, along with the private rating letter, a related private rating letter rationale report providing more in-depth analysis of the transaction, the methodology used to arrive at the private rating, and, as appropriate, discussion of the transaction's credit, legal and operational risks and mitigants. With both the private rating letter and the private rating letter rationale report the SVO would be able to determine (i) whether the private credit rating is an Eligible NAIC CRP Rating, meaning the security type is eligible to be reported on Schedule D and that it is appropriate for and NRSRO credit rating to be used to determine the regulatory treatment of the security, and (ii) whether the SVO agrees with the private credit rating. The SVO would have full discretion, based on its reasonable review of the private rating letter and the supporting rationale report, to assign an NAIC designation equivalent to the CRP PLR, to require the security to be filed for review or, to decline to assign any NAIC designation.

The SVO understands there are potential obstacles to attaining private rating letter rationale reports such as CRP confidentiality policies. However, the SVO thinks such analysis is crucial to its ability to best determine whether a rating is a satisfactory assessment of investment risk for statutory purposes due to the typical private rating letter's lack of analysis and transparency. As such the SVO is committed to working with industry and CRPs to find solutions to possible obstacles.

**3. Proposed Amendment** – The SVO proposes the following amendments to Parts One and Three of the Purposes and Procedures Manual of the Investment Analysis Office to permit the SVO to review all PL securities whether processed through a feed or submitted directly to the SVO and would require insurance company filers to provide private rating letter rationale reports for each security. The following text in red shows the proposed Purposes and Procedures Manual revisions. Updates are highlighted in yellow.

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**PART ONE**  
**POLICIES OF THE NAIC VALUATION OF SECURITIES (E) TASK FORCE**

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## FILING EXEMPTIONS

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<p style="text-align: center;"><b>POLICIES APPLICABLE TO FILING EXEMPT (FE) SECURITIES AND PRIVATE LETTER (PL) RATING SECURITIES</b></p>
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### Policy Considerations

83. In connection with the implementation of the verification procedure for PL securities, the VOS/TF acknowledges that the practices adopted by NAIC CRPs in relation to the distribution of private rating letters for what the NAIC refers to as PL securities, including their confidentiality procedures and agreements, are integral to the business models of private for-profit entities that the NAIC does not regulate and which the NAIC stands in the relation of a customer of rating services. Accordingly, the SVO, as NAIC staff, shall not be responsible for negotiating with NAIC CRPs to modify their confidentiality practices or provide data-feeds to the SVO. However, if an NAIC CRP shall determine that it is willing to modify its confidentiality provisions or provide such data-feed or an alternative process so that the SVO can obtain electronically, copies of private rating letters and private rating letter rationale reports for PL securities issued by that NAIC CRP instead of by requiring insurers to provide PDF files, then the SVO is authorized to work with the NAIC CRP to obtain and integrate the private rating letters and private rating letter rationale reports or the data-feeds into NAIC systems to create electronic processes that will permit electronic verification that the insurer-owned PL security have been assigned an NAIC CRP Eligible Credit Rating. Individual insurers and/or representatives of the insurance industry are encouraged to find ways to resolve confidentiality restrictions imposed by NAIC CRPs on the private rating letter and private rating letter rationale report or to influence the process as investors to encourage NAIC CRPs to provide the data-feeds to the SVO or alternative methods to permit the SVO to obtain NAIC CRP credit ratings and private rating letter rationale report for PL securities to be used to administer the PL securities verification procedure specified in this section.



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**PART THREE**  
**SVO PROCEDURES AND METHODOLOGY FOR PRODUCTION**  
**OF NAIC DESIGNATIONS**

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**PROCEDURE APPLICABLE TO FILING EXEMPT (FE) SECURITIES AND PRIVATE LETTER (PL)  
RATING SECURITIES**

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**PL SECURITIES**

**Effective Date of Verification Procedure for PL Securities**

9. Effective January 1, 2022, for each PL security received by the SVO either through a copy of a private rating letter or in a CRP credit rating feed, insurance companies shall be responsible for providing the SVO a copy of the related private rating letter rationale report from the applicable NAIC CRP, until such time as industry representatives and the SVO shall have established reliable procedures for obtaining the necessary information on credit ratings directly from the NAIC CRPs.
10. Effective July 1, 2018, insurance companies shall be responsible for providing the SVO copies of private rating letters for PL securities, where applicable, until such time as industry representatives and the SVO shall have established reliable procedures for obtaining the necessary information on credit ratings directly from the NAIC CRPs.
11. For **PL** Securities issued prior to January 1, 2018, if an insurance company cannot provide a copy of the rating letter to the SVO due to confidentiality concerns and the rating is not included in a CRP credit rating feed (or other form of direct delivery from the NAIC CRP), or for PL Securities issued from January 1, 2018 to January 1, 2022, if an insurance company cannot provide a copy of a “rating rationale report” to the SVO due to confidentiality or contractual reasons, the insurer shall report such securities on such securities’ General Interrogatory to be developed for this purpose (i.e., a **PL GI** security).

**Definitions**

12. For purposes of this section:
  - The phrase “private rating letter” means a letter or report issued by an NAIC CRP on its letterhead or its controlled website to an issuer or investor, obtained by an insurer in its capacity as an investor in the issuance or by following the confidentiality process established by the NAIC CRP.
  - The phrase “privately rated security” means a security issued by an issuer wherein the issuer has solicited a credit rating for the issuance from an NAIC CRP and the NAIC CRP has agreed to issue a credit rating for the issuance to be communicated to the issuer and a specified group of investors only and not publicly released via the NAIC CRP’s public data feed or website. The privately rated security is the subject of the private rating letter and is referred to herein as a private letter (PL) security.

- The phrase “private rating letter rationale report” means an analytical review of the privately rated security explaining the transaction structure, methodology relied upon, and, as appropriate, analysis of the credit, legal and operational risks and mitigants supporting the assigned NAIC CRP rating, in a report issued by an NAIC CRP on its letterhead or its controlled website to an issuer or investor, obtained by an insurer in its capacity as an investor in the issuance or by following the confidentiality process established by the NAIC CRP.

### Conditions to Filing Exemption for PL Securities Issued on or After January 1, 2018

13. PL securities are exempt from filing with the SVO for assignment of an analytically determined NAIC Designation if the security has been assigned an Eligible NAIC CRP Credit Rating, ~~and~~ the insurer verifies the rated status of the PL security to the SVO, the insurer or NAIC CRP provides the SVO with the private rating letter rationale report, and ~~the SVO concurs with the assigned Eligible NAIC CRP Credit Rating and the SVO~~ deems the privately rated security eligible to receive an NAIC Designation with an NAIC CRP Credit Rating (i.e., it is not ineligible per paragraph 21 below).
14. If the PL security is not rated by an NAIC CRP; or a credit rating is assigned that is not an Eligible NAIC CRP Credit Rating; or if the insurer cannot provide the SVO a private rating letter verifying that the assigned credit rating is an Eligible NAIC CRP Credit Rating; or the NAIC CRP cannot provide the Eligible NAIC CRP Credit Rating on the PL security to the NAIC through an electronic data feed approved by the SVO and that specifically identifies the PL securities rated by that NAIC CRP; ~~or the insurer or NAIC CRP cannot provide the private rating letter rationale report; or the SVO does not concur with the assigned Eligible NAIC CRP Credit Rating based on its review of the private letter rating rationale report;~~ or the SVO deems the privately rated security ineligible to receive an NAIC Designation with a NAIC CRP Credit Rating, the PL security is not filing exempt (i.e., it is ineligible per paragraph 21 below).
15. An insurer that owns a PL security that is not filing exempt shall either: (a) file the security with the necessary documentation with the SVO for an analytically determined NAIC Designation; or (b) self-assign an NAIC 5GI to the security and report using the Interrogatory procedure; in either case within 120 days of purchase.

### Conditions to Filing Exemption for PL Securities Issued Prior to January 1, 2018

16. **PL** securities issued prior to January 1, 2018 are exempt from filing with the SVO for assignment of an analytically determined NAIC Designation if the security has been assigned an Eligible NAIC CRP Credit Rating. If the **PL** security CRP rating is not included in the applicable CRP credit rating feed (or other form of direct delivery from the CRP) or the insurer cannot submit the private letter rating to the SVO because of confidentiality provisions, the security shall be designated **PLGI**. Insurers shall report on all such securities in a General Interrogatory with an attestation that all such securities have an Eligible CRP Credit and are reflected in the financial statements and risk-based capital calculation commensurate with that rating

### Procedure

17. The NAIC shall create systems and develop and staff administrative and operational procedures to be administered by the SVO to identify insurer-owned **PL** securities; verify whether or not the assigned credit rating is an Eligible NAIC CRP Credit Rating, review the private rating letter rationale report, and either translate that credit rating into its equivalent NAIC Designation and input the NAIC Designation for the security into the appropriate NAIC systems or notify the insurer that the security is not eligible for filing exemption.

### SVO to Administer Verification Procedures

18. It shall be the responsibility of the NAIC to create and maintain for the SVO, electronic facilities to accept: (a) electronic data-feeds provided by NAIC CRPs containing and specifically identifying the **PL** securities rated by that NAIC CRP, ~~and~~ the credit rating assigned to the **PL** securities and the supporting private rating letter rationale report; or (b) PDF files of private rating letters provided by insurers to the SVO containing the NAIC CRP credit rating for the **PL** security and a copy of the supporting private rating letter rationale report.

### The PL Process

19. It shall be the responsibility of the SVO to identify **PL** securities in the AVS+ system for insurance companies to use when reporting **PL** securities to the NAIC as part of the NAIC's Financial Statement Blank reporting process. The SVO identifies **PL** securities when it conducts the quarterly compilation of the SVO List of Securities.

### Producing NAIC Designations for PL Securities

20. The SVO shall produce NAIC Designations for securities subject to private letter ratings as follows:

- The insurance company shall file a copy of the private rating letter with the SVO if not included in the applicable NAIC CRP Rating feed(s) (or other form of direct delivery from the CRP) noted above in Conditions to Filing Exemption for PL Securities and the supporting private rating letter rationale report, if the SVO has not received it directly from the CRP, within the initial filing deadline for newly acquired securities or securities in transition (as explained in “SVO Analytical Department Symbols” in Part Two of this Manual) and each calendar year thereafter along with any changes in PL Securities rating. In instances where the PL security is included in the applicable NAIC CRP Rating feed(s), the SVO shall follow the procedure for Filing Exempt (FE) securities only after the SVO receives both the private rating letter and private rating letter rationale report either directly or through a NAIC CRP Rating feed(s), and ~~if, in its sole discretion, it concurs with the assigned Eligible NAIC CRP Credit Rating after reviewing the private rating letter rationale report and the SVO~~ deems the privately rated security eligible to receive an NAIC Designation with an NAIC CRP Credit Rating (i.e., it is not ineligible per paragraph 21 below).
- In instances where a private letter and private rating letter rationale report is filed, the SVO shall evaluate the private letter and private rating letter rationale report to determine whether the security has been assigned an Eligible NAIC CRP Rating and if the privately rated security is eligible to receive an NAIC Designation with a NAIC CRP Credit Rating (i.e., it is not ineligible per paragraph 21 below). Similar to public securities where a rating is received directly from the CRP via electronic feeds, there is a similar assumption for the PL security, that the rating meets the definition of an Eligible NAIC CRP Rating as a normal part of the CRP rating process, absent evidence to the contrary in the rating letter or private rating letter rationale report (e.g., evidence that the rating applies only to principal or interest, in a deviation from the normal CRP rating process).
- If the SVO verifies that the security has been assigned an Eligible NAIC CRP Rating and ~~if the SVO, upon review of the private rating letter rationale report and in its sole discretion, concurs with the assigned Eligible NAIC CRP Credit Rating~~ deems the privately rated security eligible to receive an NAIC Designation with a NAIC CRP Credit Rating (i.e., it is not ineligible per paragraph 21 below), it assigns an NAIC Designation in accordance with the policy and procedure specified in this Manual. The assumption in the application of this step of the procedure is that PL securities are typically assigned a credit rating by only one NAIC CRP. However, if this assumption is inaccurate for any PL security, the SVO applies the same procedure specified for FE securities.

21. If the SVO verifies that the security:

- Has been assigned a credit rating but that the credit rating is not an Eligible NAIC



CRP Credit Rating; or

- Has not been rated by an NAIC CRP; or

- Is no longer subject to a private letter rating; or
- ~~Has an assigned Eligible NAIC CRP Credit Rating that the SVO, in its sole discretion, does not concur with; or~~
- Is a type of security that is ineligible to receive an NAIC Designation with a NAIC CRP Credit Rating because it is either:
  - i. A security ineligible for filing exemption per the “Specific Population of Securities Not Eligible for Filing Exemption” in “Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities” in Part Three of this Manual. For such a security, the SVO will provide the rationale to the filer so they understand the basis for why the security will not be provided a rating.
  - ii. A security for which the SVO does not believe is within the scope of SSAP No. 26R or SSAP No. 43R. For such a security, the SVO will provide an accounting analysis, to the filer, on why they do not believe the security is within the scope of SSAP No. 26R or SSAP No. 43R so the filer understands the SVO’s rationale and allows for the issuer to challenge the SVO’s rationale with the SVO, their regulator, NAIC accounting staff or SAPWG, as appropriate.

The SVO shall notify the insurer that the security is not eligible for filing exemption. The insurance company shall then either file that security and necessary documentation with the SVO for an independent credit assessment or assign an **NAIC 5GI** Regulatory Designation to the security in the related Interrogatory.

22. An **NAIC 5GI** Designation may also be used in connection with the designation of **PL** securities rated by an NAIC CRP (i.e., for private letter ratings issued on or after January 1, 2018) when the documentation is not available for the SVO to assign an NAIC Designation, or for private letter ratings issued from January 1, 2018 to January 1, 2022, if an insurance company does not provide a copy of a “rating rationale report” to the SVO and there are no confidentiality or contractual reasons, or for any private letter ratings issued after January 1, 2022 for which a rating rationale report is not submitted to the SVO. For purposes of this section, the documentation is not available for the SVO to assign an NAIC Designation if the NAIC CRP credit rating is not included in the applicable CRP credit rating feed (or other form of direct delivery from the NAIC CRP) and the insurer is unable to provide a copy of the private letter rating documentation, including the private rating letter rationale report, necessary for the SVO to assign an NAIC Designation.



To: NAIC Securities Valuation Office & NAIC Capital Markets & Investment Analysis Office

From: Dale Bruggeman, Chair of the Statutory Accounting Principles (E) Working Group

Date: January 22, 2020

Re: Residual Risk Threshold for Credit Tenant Loan (CTL) Investments

On Nov. 12, the Working Group continued discussion of agenda item 2020-24: Accounting and Reporting of Credit Tenant Loans and directed that “conforming” CTLs shall remain in scope of *SSAP No. 43R—Loan-Backed and Structured Securities* with reporting to occur on Schedule D-1. On Dec. 28, the Working Group provided a limited-time provision to permit non-conforming CTLs continued D-1 reporting if they are filed with the SVO by February 15, 2021. With this provision, nonconforming CTLs reported on Schedule D-1 that have not received an SVO-assigned designation shall be disclosed in Note 1 as if a permitted practice.

As you are likely aware, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) specifies many criteria required for an investment to qualify as a conforming CTL. In addition to a legal and structural analysis, one such standard is a maximum threshold of a 5% residual asset risk. The residual asset risk limit of 5% was established in 1994 from the Invested Asset Working Group. As this committee no longer exists, this memorandum requests your comments on the following:

- Whether it is appropriate to revisit the 5% residual asset risk threshold as a restriction for conforming CTLs.
- If applicable, a recommendation of an appropriate residual risk threshold.
- Whether other mechanisms or compensating controls (beyond a residual risk insurance policy) could be incorporated as a mitigating factor for CTLs that exceed the 5% residual risk threshold (or a threshold as recommended).
- A listing of the nonconforming CTLs that were filed with the SVO in accordance with the direction of Interpretation (INT) 20-10. Please include high level details including outstanding principal and NAIC designation assigned by the SVO.

In addition, the Working Group is also requesting information, to the extent possible using best efforts, on 1) how many CTLs originally exceeded the residual risk threshold but were later considered as “conforming” due to mitigating factors, and 2) the nature of those factors (i.e. a residual risk insurance policy).

Thank you for considering this request. If you have questions, please contact Julie Gann, NAIC staff of the Statutory Accounting Principles (E) Working Group.

Attachments: SAPWG Agenda Item 2020-24 & INT 20-10

Cc: Julie Gann, Robin Marcotte, Fatima Sediqzad, Jake Stultz, Jim Pinegar, Charles Therriault, Marc Perlman, Eric Kolchinsky

G:\SECVAl\DATA\Vos-tf\Meetings\2021\February\VOSTF 02-18-2021\03 - Referral from SAPWG on Non-Conforming CTLs\2021-029.01 SAPWG to SVO - CTL Residual Risk.docx

**Statutory Accounting Principles (E) Working Group  
 Maintenance Agenda Submission Form  
 Form A**

**Issue:** Accounting and Reporting of Credit Tenant Loans

**Check (applicable entity):**

	P/C	Life	Health
Modification of Existing SSAP	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
New Issue or SSAP	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Interpretation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

**Description of Issue:**

This agenda item intends to clarify the reporting of credit tenant loans (CTL) for statutory accounting. Although this is an investment (that if meeting certain criteria) may have been historically captured in *SSAP No. 43R—Loan-Backed and Structured Securities*, due to recent discussions at the Valuation of Securities (E) Task Force, in order to provide timely guidance, it was identified that this issue needs to be considered separately outside of the substantive SSAP No. 43R project. As the SSAP No. 43R project is a substantive assessment, with various aspects being considered, it is noted that the conclusion of that project may extend beyond the timeframe for which clarity on CTLs is needed.

This agenda item focuses on credit tenant loans. There are other variations of similar investments that should also be specifically named / addressed in the AP&P Manual. These include ground lease financings as well as other lease-backed (non-ABS) securities. NAIC staff recommends that the Working Group first consider CTLs, with separate subsequent consideration of other structures.

Pursuant to guidance in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*:

Mortgage loans that are made primarily in reliance on the credit standing of a major tenant, structured with an assignment of the rental payments to the lender with real property pledged as collateral in the form of a first lien, are referred to as a Credit Tenant Loan. (*Staff Note – This overall definition also matches the NAIC Model 280: Investments of Insurers Model Act (Defined Limits Version)*).

**Credit Tenant Loan (CTL)** – A CTL is a mortgage loan made primarily in reliance on the credit standing of a major tenant, structured with an assignment of the rental payments to the lender with real property pledged as collateral in the form of a first lien. This Manual identifies four categories of CTLs as eligible for reporting on Schedule D conditioned on an SVO determination that the transaction meets the criteria specified by the VOS/TF for Schedule D treatment. A transaction that purports to be a Credit Tenant Loan, including one that is assigned a credit rating by an NAIC CRP, is not eligible for Schedule D reporting unless the SVO confirms that the transaction is eligible for Schedule D reporting and assigns the transaction an NAIC Designation.

It has been long-standing practice for CTLs to be filed with the NAIC SVO for review and assessment. If the SVO identified that the CTL qualifies under the SVO’s legal and structural analysis (which reflects bond characteristics) and meets certain other criteria (such as minimal residual real-estate risk), then it has been granted special treatment and reported in scope of SSAP No. 43R on schedule D. If the CTL did not qualify under the SVO provisions or if it was not filed with the SVO, it would not qualify to be reported as a bond. These CTLs are often referred to as “non-conforming CTLs.” It has been presumed that a non-conforming CTL would be considered a mortgage loan and reported in scope of *SSAP No. 37—Mortgage Loans*.

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The Valuation of Securities (E) Task Force has recently been discussing CTLs as it was identified that CTLs that were not submitted to the SVO and/or did not qualify under the SVO's structural and legal analysis were being reported on Schedule D with filing exempt designations. Although this identification resulted with discussion at the Task Force on the existing process, it was also noted that the overall statutory accounting guidance is not clear. The following elements have been identified as potential accounting and reporting issues:

1. There is no clear guidance in the *Accounting Practices & Procedures Manual* that SVO-identified conforming CTLs are in scope of SSAP No. 43R. It is noted that the CTL structure does not qualify within the SSAP No. 43R definition of a loan-backed and structured security (LBSS), and all that is currently included in SSAP No. 43R is a generic reference to "credit-tenant loans" as an example of an "all other" loan-backed and structured security. This reference is in paragraph 27.b of SSAP No. 43 in the section that addresses "designation guidance."
2. It is presumed that non-SVO-identified CTLs would have historically been reported as mortgage loans. However, SSAP No. 37 explicitly excludes "securities" from the scope of the standard. Due to the structure of CTLs, and as they have CUSIPs, there is a question whether they are a "security" which would then specifically exclude CTL's from the mortgage loan guidance.
3. It has been identified that if non-conforming CTLs are reported as mortgage loans, the RBC calculation may be considered punitive for these specific designs. This is because the assessment of a CTL is based on the credit quality of the major tenant, whereas the RBC calculation factors for mortgage loans is a loan-to-value (LTV) assessment. As the RBC calculation does not have an alternative process for CTL structures, under the LTV process, these loans receive high RBC charges.
4. If the non-conforming CTLs are not reported on schedule D and not reported as mortgage loans, they would be captured on Schedule BA – Other Long-Term Invested Assets. Although there are certain classes of assets that could be reported with NAIC designations on Schedule BA, assets with underlying characteristics of mortgage loans do not currently have this capability. As such, if reported under this Schedule BA category under current provisions, these items would receive a 20% RBC for property/casualty and health filers and would receive a 30% charge for life filers. Even if provisions were incorporated to permit NAIC designations for this class of asset (or direct reporting within a different reporting line), this would only allow life insurers to receive a reduction in RBC. There would be no benefit for property/casualty and health filers under existing RBC provisions.

In order to fully assess the proper accounting and reporting, this agenda item presents the following key characteristics of CTLs:

- A CTL generally is long-term in nature in comparison to a commercial mortgage. So, whereas a commercial mortgage loan may be between 5-10 years, a CTL could be between 15-40 years of fixed payments that correspond to the term of the lease and the loan.
- The CTL is structured based on the credit-quality of the corporate tenant which is obligated to pay rent regardless of property casualty, condemnation or obsolescence and to pay all expenses associated with the property, such as taxes, maintenance and utilities. The investment, however, is secured with collateral through a mortgage on the property. With this structure, the reporting entity receives a steady cash flow stream with the additional protection of real estate collateral.
- Conforming CTLs are generally structured to be fully amortized over the term of the loan and lease; however, they are illiquid investments. This principal amortizing component is a key element of the

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requirements in determining whether a CTL meets the SVO requirements in support of bond classification / NAIC designation. (Technically, if the structure is not substantively amortized over the term, then it is not a Schedule D eligible CTL, per the P&P Manual. However, the phrase “non-conforming CTL” is used to describe the general structure of the transaction.) To provide simple examples (ignoring investment returns or interest payments):

- Example 1: If a CTL investment reflected \$1,500,000, with the investor receiving \$100,000 in annual cash payments over a 15-year lease/loan term, at conclusion of the investment, the principal balance would have been returned to the investor. Although the underlying property would have been provided as collateral as part of the CTL agreement, with the structure of the investment, there is little risk that the property would be transferred to the reporting entity at maturity to satisfy a remaining principal amount due. This is referred to as “residual risk.” The SVO parameters permit a slight amount of residual risk (e.g., 5%) in conforming CTLs. If the investment retains a greater amount of residual risk, then additional mitigation elements must be included in the structure for an SVO “conforming CTL” designation.
- Example 2: If a CTL investment reflected \$1,500,000, with the investor receiving \$600,000 in total cash payments over a 15-year lease/loan term, at conclusion of the investment, the reporting entity investor would be due \$900,000. If the structure was not renewed or refinanced with the tenant (or a new tenant), then the reporting entity investor would receive ownership of the building in lieu of the remaining principal amount owed. The reporting entity investor would then have to sell the building to recoup their investment. This structure reflects a level of residual risk that has been historically deemed unacceptable for bond reporting under the SVO parameters. Rather, this structure has been historically considered to reflect a mortgage loan at inception, with reclassification as real estate if the reporting entity received the property at the conclusion of the investment maturity.

The focus of this agenda item is to inquire whether the conforming CTLs (such as example 1) should be captured in scope of SSAP No. 43R or whether these investments should be captured in SSAP No. 21R—Other Admitted Assets. This agenda item is not proposing that structures that do not conform to current requirements (such as example 2) be considered in scope of SSAP No. 43R. This agenda item also inquires whether structures that are not conforming CTLs (such as example 2) should be reported as mortgage loans or whether these structures should be captured in SSAP No. 21R. This agenda item is not proposing to reconsider the existing SVO guidelines in determining whether a CTL is “conforming” and in determining what is considered to be a suitable amount of “residual risk.” If there is a desire to reassess these provisions, NAIC staff would recommend a separate project with the Task Force, after concluding on desired reporting location and governing SSAP, to review these parameters.

Although it is understood that historical practice has permitted certain SVO verified CTLs that meet legal and structural analyses to be reported on Schedule D, there is a question whether these investments reflect bonds or securitized assets that should be included on the bond schedule. If preferred by the Working Group, revisions can be considered to remove these items from potential Schedule D reporting and instead capture these investments in scope of SSAP No. 21R. Some elements to consider in determining whether SSAP No. 21R would be more appropriate:

- If captured in scope of SSAP No. 21R, all CTLs will be reported in the same schedule, regardless of whether they are considered “conforming” or “non-conforming” CTLs. (In other words, the same reporting schedule would occur regardless of the NAIC SVO assessment.) This reporting process would likely result with improved identification and assessment of CTL investments in the financial statements. Under the current

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process, since CTLs are bifurcated across reporting schedules, it is not possible to identify the full extent an insurer is invested in CTLs (regardless if confirming or non-confirming).

- If captured in scope of SSAP No. 21R, CTLs could still be filed with the NAIC SVO for the legal and structural analysis and, if qualifying, to obtain an NAIC designation. For these “conforming” CTLs, revisions could be incorporated to permit the NAIC designation to be reported on Schedule BA. This NAIC designation could be used by life insurers to obtain an improved RBC designation. (Although the improved RBC is not an option under the current RBC formula for non-life entities, from information gathered, most CTL holders are life insurers.)
- Reporting CTLs in scope of SSAP No. 21R would be consistent with previous decisions of the SAPWG to not report non-bond items as bonds simply for RBC purposes. It would also be consistent with the policy statement that obtaining an NAIC designation does not direct statutory accounting or reporting. Pursuant to this policy statement, obtaining an NAIC designation does not change an investment’s applicable SSAP, annual or quarterly reporting schedule or override other SSAP guidance required for the investment to be an admitted asset. This policy statement does identify that there are limited situations in which an SVO-listing could be used for classification purposes that focuses on the underlying structure of the investment. If conforming CTL investments are retained in SSAP No. 43R (and not moved to SSAP No. 21R), it would be recommended that CTLs that meet the SVO structural analysis be captured on a listing that could be referred to in the scope section of SSAP No. 43R. It is noted that the recent issues involving non-conforming CTLs seem to originate from an interpretation that obtaining a CRP rating would allow entities to report these structures as bonds on Schedule D through the filing exemption process. This assessment is incorrect under existing statutory accounting guidance and the existing policy statement.
- Reporting CTLs in scope of SSAP No. 21R would seemingly be consistent with the decision made for structured settlements in 2018. Although structured settlements and CTLs are vastly different investments, they both represent an investment, that is not a bond, but reflects an investment in a cash flow stream that is subject to the underlying credit quality of the payer.

On May 29, 2020, the Valuation of Securities (E) Task Force submitted a referral to the Working Group to permit non-conforming CTLs that receive an NAIC designation from the SVO to be considered in scope of SSAP No. 43R. Excerpts of this referral have been provided below:

The Task Force is referring this memo and proposed amendment to the Statutory Accounting Principles (E) Working Group and **requesting the Working Group affirm that they would consider these Non-conforming CTLs to have the characteristics of a bond if assigned an NAIC Designation by the SVO staff**. Like the referral from earlier this year on GLFs, these Non-conforming Credit Tenant Loan (CTL) Transactions have historically been reported under the Accounting Practices & Procedures Manual’s SSAP No. 43R – Loan-Backed and Structured Securities under Paragraph 27, b as a type of CTL. The SVO staff recommends affirming that treatment only if the SVO staff can assign an NAIC Designation.

The edits noted in the Task Force referral are revisions to the *Purposes and Procedures Manual (P&P)* to affirm the Task Force’s role in making all decisions on the use of CRP ratings and provides guidance to insurance company filers on what to do if they are uncertain about the filing procedure for a particular security or class of securities.

NAIC staff highlights that it would be inconsistent with the *Policy Statement on Coordination of the AP&P Manual and the P&P Manual of the NAIC IAO* to permit CTLs to be classified as a bond simply in accordance with an NAIC designation / CRP rating. However, the provisions in the Policy Statement does identify that such classifications can occur based on an SVO structural assessment of an investment. NAIC SAPWG staff has

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confirmed with the SVO staff that the review and assignment of an NAIC designation for CTLs requires a structural assessment, and they only receive an NAIC designation if the CTL possess bond characteristics.

### Existing Authoritative Literature:

#### *SSAP No. 37—Mortgage Loans*

2. **A mortgage loan is defined as a debt obligation that is not a security, which is secured by a mortgage on real estate.** In addition to mortgage loans directly originated, a mortgage loan also includes mortgage loans acquired or obtained through assignment, syndication or participation<sup>1</sup>. Investments that reflect “participating mortgages,” “mortgage loan fund,” “bundled mortgage loans<sup>2</sup>” or the “securitization of assets” are not considered mortgage loans within scope of this SSAP.
- a. A security is a share, participation, or other interest in property or in an entity of the issuer or an obligation of the issuer that has all of the following characteristics:
- i. It is either represented by an instrument issued in bearer or registered form, or if not represented by an instrument, is registered in books maintained to record transfers by or on behalf of the issuer.
- ii. It is of a type commonly dealt in on securities exchanges or markets or, when represented by an instrument, is commonly recognized in any area in which it is issued or dealt in as a medium for investment.

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<sup>1</sup> Examples of agreements intended to be captured within this statement:

- a. Reporting entity is a “co-lender” in a single mortgage loan agreement that identifies more than one lender (which includes the reporting entity) with the real estate collateral securing all lenders identified in the agreement. For these single-mortgage loan agreements, each lender is incorporated directly into the loan documents. The key differentiating characteristic of a mortgage loan provided under a group “mortgage loan co-lending agreement” rather than a solely owned mortgage loan is that no one lender of the lending group may unilaterally foreclose on the mortgage. With these agreements, the lenders must foreclose on the mortgage loan as a group.
- b. Reporting entity has a “participation agreement” to invest in a single-mortgage loan. The reporting entity is not the lender of record named as a payee on the mortgage loan, but the lender of record sells a portion of the mortgage loan to the reporting entity through an assignment or participation interest under the participation agreement. Under a participation agreement, the reporting entity acquires an undivided interest in the single mortgage loan proceeds to be received by the lender of record. Under a participation agreement, single mortgage loan proceeds include the periodic mortgage loan principal and interest payments received by the lender of record, and all rights and proceeds received in the foreclosure of a mortgage, deed of trust, deed in lieu of foreclosure, or other similar proceeding by the lender of record. The amount of the proceeds to be received by the reporting entity is based on the ratio of its participation interest to the then-outstanding single mortgage loan balance. To qualify as a mortgage loan under the scope of this statement, the reporting entity must have a signed participation agreement with the lender of record named in the mortgage loan, the financial rights and obligations of the reporting entity under the participation agreement are the same as the lender of record, the reporting entity’s participation interest in the single mortgage loan proceeds must be pari-passu with the lender of record named on the mortgage loan agreement, and the participation agreement must be properly and promptly recorded on the lender or record’s books and records.

<sup>2</sup> The scope of this SSAP is limited to single mortgage loan agreements. Although single mortgage loan agreements can potentially have more than one lender (e.g., co-lenders/participations) and more than one borrower (such as in a tenancy-in-common arrangement), the concept of a “single mortgage loan” does not include arrangements in which a reporting entity acquires more than one mortgage loan in a sole transaction. (For example, if a reporting entity was to acquire an interest in a “bundle” of mortgage loans with various unrelated borrowers and collateral, this agreement would be outside of the scope of this SSAP. However, a bundle of mortgage loans does not include a “bulk purchase” where the reporting entity’s interest in each mortgage loan is legally separate and divisible and the purchase just facilitates the acquisitions of multiple single mortgage loan agreements.)



- iii. It either is one of a class or series or by its terms is divisible into a class or series of shares, participations, interests, or obligations.

***SSAP No. 43R—Loan-Backed and Structured Securities***

*(Excerpts from scope guidance)*

2. Loan-backed securities are defined as securitized assets not included in structured securities, as defined below, for which the payment of interest and/or principal is directly proportional to the payments received by the issuer from the underlying assets, including but not limited to pass-through securities, lease-backed securities, and equipment trust certificates.
3. Structured securities are defined as loan-backed securities which have been divided into two or more classes for which the payment of interest and/or principal of any class of securities has been allocated in a manner which is not proportional to payments received by the issuer from the underlying assets.
4. Loan-backed securities are issued by special-purpose corporations or trusts (issuer) established by a sponsoring organization. The assets securing the loan-backed obligation are acquired by the issuer and pledged to an independent trustee until the issuer's obligation has been fully satisfied. The investor only has direct recourse to the issuer's assets, but may have secondary recourse to third parties through insurance or guarantee for repayment of the obligation. As a result, the sponsor and its other affiliates may have no financial obligation under the instrument, although one of those entities may retain the responsibility for servicing the underlying assets. Some sponsors do guarantee the performance of the underlying assets.
  - a. In determining whether a loan-backed structure is a related party investment, consideration shall be given to the substance of the transaction, and the parties whose action or performance materially impacts the insurance reporting entity holding the security. For example, although a loan-backed security may be acquired from a non-related issuer, if the assets held in trust predominantly<sup>3</sup> reflect assets issued by affiliates of the insurance reporting entity, and the insurance reporting entity only has direct recourse to the assets held in trust, the transaction shall be considered an affiliated investment, and the transaction shall also subject to the accounting and reporting provisions in *SSAP No. 25—Affiliates and Other Related Parties*.
5. Mortgage-referenced securities do not meet the definition of a loan-backed or structured security but are explicitly captured in scope of this statement. In order to qualify as a mortgage-referenced security, the security must be issued by a government sponsored enterprise<sup>4</sup> in the form of a "credit risk transfer" in which the issued security is tied to a referenced pool of mortgages. These securities do not qualify as "loan-backed securities" as the pool of mortgages are not held in trust and the amounts due under the investment are not backed or secured by the mortgage loans. Rather, these items reflect instruments in which the payments received are linked to the credit and principal payment risk of the underlying mortgage loan borrowers captured in the referenced pool of mortgages. For these instruments, reporting entity holders

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<sup>3</sup> In applying this guidance, a reporting entity is not required to complete a detailed review of the assets held in trust to determine the extent, if any, the assets were issued by related parties. Rather, this guidance is a principle concept intended to prevent situations in which related party transactions (particularly those involving affiliates) is knowingly captured in a SSAP No. 43R structure and not identified as a related party transaction (or not reported as an affiliated investment on the investment schedule) because of the involvement of a non-related trustee or SSAP No. 43R security issuer. As identified in *SSAP No. 25—Affiliates and Other Related Parties*, it is erroneous to conclude that the inclusion of a non-related intermediary, or the presence of non-related assets in a structure predominantly comprised of related party investments, eliminates the requirement to identify and assess the investment transaction as a related party arrangement.

<sup>4</sup> Currently, only Fannie Mae and Freddie Mac are the government sponsored entities that issue qualifying mortgage-referenced securities. However, this guidance would apply to mortgage-referenced securities issued by any other government sponsored entity that subsequently engages in the transfer of residential mortgage credit risk.

may not receive a return of their full principal as principal repayment is contingent on repayment by the mortgage loan borrowers in the referenced pool of mortgages. Unless specifically noted, the provisions for loan-backed securities within this standard apply to mortgage-referenced securities.

6. Investments within the scope of this statement are also subject to the provisions and disclosure requirements of SSAP No. 25 if the SSAP No. 43R transaction is a related party arrangement<sup>5</sup>. Loan-backed and structured securities meet the definition of assets as defined in SSAP No. 4—Assets and Nonadmitted Assets and are admitted assets to the extent they conform to the requirements of this statement and SSAP No. 25.

7. The scope of this statement encompasses all types of loan-backed and structured securities, including, but not limited to, the following:

- a. Loan-backed and structured securities acquired at origination,
- b. Loan-backed and structured securities acquired subsequent to origination for which it is probable, at acquisition, that the reporting entity will be able to collect all contractually required payments receivable, and are accounted for at acquisition under SSAP No. 103R,
- c. Loan-backed and structured securities for which it is probable, either known at acquisition or identified during the holding period<sup>6</sup>, that the reporting entity will be unable to collect all contractually required payments receivable, and
- d. Transferor's beneficial interests in securitization transactions that are accounted for as sales under SSAP No. 103R and purchased beneficial interests in securitized financial assets<sup>7</sup>.

### Designation Guidance

27. For RMBS/CMBS securities within the scope of this statement, the initial NAIC designation used to determine the carrying value method and the final NAIC designation for reporting purposes is determined using a multi-step process. The *Purposes and Procedures Manual of the NAIC Investment Analysis Office* provides detailed guidance. A general description of the processes is as follows:

- a. Financial Modeling: The NAIC identifies securities where financial modeling must be used to determine the NAIC designation. NAIC designation based on financial modeling incorporates the insurers' carrying value for the security. For those securities that are financially modeled, the insurer must use NAIC CUSIP specific modeled breakpoints provided by the modelers in determining initial and final designation for these identified securities. Securities where modeling results in zero expected loss in all scenarios are automatically considered to have a final NAIC designation of NAIC 1, regardless of the carrying value. The three-step process for modeled securities is as follows:

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<sup>5</sup> As discussed in paragraph 4.a. of this statement, a SSAP No. 43R security may still be considered a related party transaction even if the asset trustee or security issuer is a non-related party.

<sup>6</sup> Securities classified within the type of paragraph 7.a. or 7.b. may be required to change classification to type 6.c. when it becomes probable that the reporting entity will be unable to collect all contractually required payments receivable.

<sup>7</sup> The accounting requirements related to these types of securities included in paragraphs 22-25 shall be determined at acquisition or initial transfer.

- i. Step 1: Determine Initial Designation – The current amortized cost (divided by remaining par amount) of a loan-backed or structured security is compared to the modeled breakpoint values assigned to the six (6) NAIC designations for each CUSIP to establish the **initial** NAIC designation.
  - ii. Step 2: Determine Carrying Value Method – The carrying value method, either the amortized cost method or the lower of amortized cost or fair value method, is then determined as described in paragraph 26 based upon the initial NAIC designation from Step 1.
  - iii. Step 3: Determine Final Designation – The final NAIC designation that shall be used for investment schedule reporting is determined by comparing the carrying value (divided by remaining par amount) of a security (based on paragraph 27.a.ii.) to the NAIC CUSIP specific modeled breakpoint values assigned to the six (6) NAIC designations for each CUSIP. This final NAIC designation shall be applicable for statutory accounting and reporting purposes (including establishing the AVR charges). The final designation is not used for establishing the appropriate carrying value method in Step 2 (paragraph 27.a.ii.).
- b. All Other Loan-Backed and Structured Securities: For loan-backed and structured securities not subject to paragraphs 27.a. (financial modeling) follow the established designation procedures according to the appropriate section of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. The NAIC designation shall be applicable for statutory accounting and reporting purposes (including determining the carrying value method and establishing the AVR charges). The carrying value method is established as described in paragraph 26. **Examples of these securities include, but are not limited to,** mortgage-referenced securities, equipment trust certificates, **credit tenant loans (CTL)**, 5\*/6\* securities, interest only (IO) securities, securities with CRP ratings (excluding RMBS/CMBS), and loan-backed and structured securities with SVO assigned NAIC designations.

***Note: This is the only reference to credit tenant loans in the AP&P Manual.***

**Activity to Date (issues previously addressed by the Working Group, Emerging Accounting Issues (E) Working Group, SEC, FASB, other State Departments of Insurance or other NAIC groups):** The following items are noted as recent actions / projects by the Working Group:

- In agenda items 2018-22 and 2016-39, the Working Group clarified the scope guidance in SSAP No. 37. With these revisions (reflected in the cited guidance), the Working Group has clarified that the focus of SSAP No. 37 is on direct, single mortgage loan agreements that are not securities. These revisions have clarified that the scope of the SSAP does not include funds, securitizations, or “bundles” of mortgage loans.
- The Working Group has a current project to substantively review and revise SSAP No. 43R. Pursuant to agenda item 2019-21, the original focus was on “equity” related items (such as collateralized fund obligations), but the scope of the project has been expanded to include a complete review of SSAP No. 43R. The initial discussion draft issue paper was exposed in March 2020 with a comment period ending July 31, 2020. This initial exposure focused initial review of broad groupings of assets and did not address investments addressed in the *Purposes and Procedures Manual*. The issue paper noted that these VOSTF-related items were pending development and would be addressed in subsequent exposures.

**Information or issues (included in *Description of Issue*) not previously contemplated by the Working Group:**  
None

**Convergence with International Financial Reporting Standards (IFRS): Not Applicable**

**Staff Recommendation:**

NAIC Staff recommends that the Working Group move this item to the active listing, initially categorized as nonsubstantive and expose the agenda item to solicit comment before directing NAIC staff on the desired guidance for CTLs. There are two general options:

- **Option 1: SSAP No. 43R for Conforming CTLs (this includes CTLs With SVO-Identified Bond Characteristics Acquired Prior to Jan. 1, 2020 as detailed in the P&P Manual)** – With this option, statutory accounting will continue with historical application and keep CTLs that are identified to have bond characteristics, after review by the SVO, in scope of SSAP No. 43R and reported on Schedule D as bonds. If selecting this option, the Working Group should also advise if they would prefer for the nonqualifying CTLs to be in scope of *SSAP No. 37—Mortgage Loans* and reported on Schedule B, or if they want these investments to be considered an “other invested asset” under SSAP No. 21 and reported on Schedule BA. (Note: The SVO will only review non-conforming CTLs held prior to Jan. 1, 2020 for bond characteristics. As such all non-conforming CTLs acquired after Jan. 1, 2020 will not be in scope of SSAP No. 43R.)

If selecting this option, NAIC staff will propose edits to SSAP No. 43R to explicitly include in scope CTLs that are included on an SVO-Identified listing based on a structural analysis. Furthermore, revisions will be proposed to either SSAP No. 37 or *SSAP No. 21R—Other Invested Assets* to capture CTL type structures that are not on the SVO identified listing.

**Option 2: SSAP No. 21 for All CTLs** – With this option, statutory accounting revisions will be proposed to capture all CTLs in scope of *SSAP No. 21—Other Invested Assets* and reported on Schedule BA. With this approach, all CTLs will be reported on the same schedule, and revisions will be proposed to allow CTLs that are reviewed and approved by the NAIC SVO to be reported with an NAIC designation. This process will be similar to the existing approach for other non-bond items reported on Schedule BA that have underlying characteristics of fixed income instruments. With this approach, there will be no need to reference an SVO-Identified listing of qualifying CTLs in SSAP No. 21R. Pursuant to the *Purposes and Procedures Manual*, CTLs will not qualify as filing exempt, and a CTL would need an SVO-provided NAIC designation if there was a desire to obtain a more favorable RBC. (Only CTLs the SVO determines qualify to receive an NAIC designation will be assigned one and will be identified on a separate listing maintained and published by the SVO.) (Under existing RBC parameters, the ability for a more favorable RBC on Schedule BA based on NAIC designation is only permitted for life entities.)

**In addition to exposing a direction, NAIC staff recommends notifying the Valuation of Securities (E) Task Force of this agenda item in response to their referral. With this notification, NAIC staff will request further confirmation that an SVO-Listing could be developed to capture the CTLs that meet the SVO’s structural and legal analysis and possess bond characteristics.**

**Staff Review Completed by:**

Julie Gann - NAIC Staff  
June 2020

**Status:**

On July 30, 2020, the Statutory Accounting Principles (E) Working Group moved this item to the active listing, categorized as nonsubstantive, and exposed this agenda item with a request for comments on the two general options

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for the accounting treatment of credit tenant loans (CTL). Notification will also be sent to the Valuation of Securities (E) Task Force of this agenda item in response to their referral. With this notification, NAIC staff will request further confirmation that a SVO-Listing could be developed to capture the CTLs that meet the SVO's structural and legal analysis and possess bond characteristics.

### **Proposed Language – October 2020**

The following proposed edits intend to reflect guidance if the Working Group directs for Option 1, with conforming CTLs in SSAP No. 43R. Language is proposed to show the edits that could occur if non-conforming CTLs are directed for Schedule BA or in scope of SSAP No. 37. If the Working Group directs Option 1 with an exposure, only the edits that correspond to the Working Group direction will be exposed. (For example, if the Working Group directs Option 1 with non-conforming in BA, then the edits drafted for SSAP No. 37 will not be exposed.)

### **Proposed Revisions to SSAP No. 43R—Loan-Backed and Structured Securities:**

#### SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for investments in loan-backed and structured securities. Items captured in scope of this statement are collectively referred to as loan-backed securities. The scope of this statement includes:
  - a. Loan-backed and structured securities defined in paragraphs 2-4 and 7.
  - b. Mortgage-referenced securities defined in paragraph 4.
  - c. Retained beneficial interests from the sale of loan-backed and structured securities in accordance with *SSAP No. 103R—Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*.
  - d. Credit tenant loans (CTLs), which qualify for bond treatment, pursuant to a structural analysis as identified in Part 3 of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. CTLs that do not qualify are referred to as “non-conforming” CTLs and shall be reported on Schedule BA: Other Long-Term Invested Assets. With this classification, certain reporting entities can file the instrument with the NAIC SVO for a credit analysis and report the non-conforming CTL with the SVO-assigned NAIC designation. Although the structure of CTL does not permit reporting in scope of SSAP No. 43R (on Schedule D-1), the credit assessment reported on Schedule BA can be used to influence risk-based capital charges.

*Staff Note: If the Working Group directs mortgage loans reporting for non-conforming CTLs instead of Schedule BA, the following replacement paragraph for 1.d. would be utilized:*

Credit tenant loans (CTLs), which qualify for bond treatment, pursuant to a structural analysis as identified in Part 3 of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. CTLs that do not qualify are referred to as “non-conforming” CTLs and are captured in scope of SSAP No. 37—*Mortgage Loans*.

- e. Ground lease financing (GLF) transactions, which qualify for bond treatment, pursuant to a structural analysis as identified in Part 3, of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*.

Although the recommendation is for Schedule BA, if the Working Group directs non-conforming CTLs to SSAP No. 37—Mortgage Loans, the following language has been drafted for consideration: (This language will be removed if the Working Group proceeds with the Schedule BA reporting proposal.)

#### SCOPE OF STATEMENT

1. This statement establishes statutory accounting principles for the accounting and reporting of mortgage loans and related fees. The scope of this statement includes:
  - a. Mortgage loans defined in paragraph 2.
  - b. Credit tenant loans (CTLs) which do not qualify for bond treatment, pursuant to a structural analysis as identified in Part 3 of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*. CTLs that qualify for bond reporting are published on (add SVO website reference). (CTLs are captured in scope of this statement although they may meet the “security” definition reflected in paragraph 2 unless they qualify for bond reporting under the SVO structural analysis. By definition, a credit tenant loan is a mortgage loan.)

#### Status:

On November 12, 2020, the Statutory Accounting Principles (E) Working Group took the following actions:

1. Confirmed that conforming CTLs will remain in scope of SSAP No. 43R and reported on D-1;
2. Directed a referral to the SVO to request information on the residual risk percentage permitted to be considered a conforming CTL; and
3. Permit nonconforming CTLs filed with the SVO that receive an SVO-assigned NAIC designation to be reported on Schedule D-1. If the nonconforming CTLs are not filed or have not received a NAIC SVO designation before the March 1, 2021, filing date, the securities shall be reported on Schedule BA.

On December 4, 2020, due to the number of questions requesting clarification on the motion, the Working Group exposed INT 20-10: Reporting Nonconforming Credit Tenant Loans.

On December 28, 2020, the Statutory Accounting Principles (E) Working Group adopted INT 20-10: Reporting Nonconforming Credit Tenant Loans, temporarily allowing continued D-1 reporting of nonconforming CTLs if they are filed with the SVO by February 15, 2021. With this provision, nonconforming CTLs reported on Schedule D-1 that have not received an SVO-assigned designation shall be disclosed in Note 1 as if a permitted practice.

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**INT 20-10**

**Interpretation of the Statutory Accounting Principles Working Group**

**INT 20-10: Reporting Nonconforming Credit Tenant Loans**

**INT 20-10 Dates Discussed**

Evote to Expose November 18, 2020; December 18, 2020; Evote to Adopt December 28, 2020

**INT 20-04 References**

*SSAP No. 43R—Loan-Backed and Structured Securities*

*NAIC Policy Statement on Coordination of the Accounting Practices and Procedures Manual and the Purposes and Procedures Manual of the Investment Analysis Office*

**INT 20-10 Issue**

1. During the Statutory Accounting Principles (E) Working Group meeting on November 12, 2020, the Working Group discussed and deferred final decision on inconsistencies in the reporting of “nonconforming” credit tenant loans (CTLs) currently reported on Schedule D-1 and directed reporting exceptions for year-end 2020. Due to subsequent questions, this interpretation has been issued to detail the provisions provided and clarify the reporting of CTLs in the year-end 2020 statutory financial statements.

**INT 20-10 Discussion**

2. As detailed in agenda item 2020-24, some reporting entities have reported CTLs that do not qualify as “conforming” CTLs per the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) on Schedule D-1: Long-Term Bonds. CTLs that do not qualify under the P&P Manual structural requirements are noted as “nonconforming” CTLs. During the November 12 discussion, the Working Group deferred final guidance on the reporting of nonconforming CTLs. This deferral was supported as the Working Group has a separate project to assess investments that are captured on Schedule D-1. With this project, it was identified that it would be undesirable to require an investment that is currently being reported on Schedule D-1 to be moved to a different schedule if there was potential for that investment to subsequently qualify for Schedule D-1.

3. Although the Working Group deferred final conclusion on the reporting of nonconforming CTLs, it was identified that the long-standing guidance detailed in the P&P Manual only permits CTLs that met certain structural criteria, which is verified by the SVO, to be reported on Schedule D-1. Under this existing guidance, these conforming CTLs are also prohibited from using CRP ratings in determining NAIC designation but are required to utilize SVO-assigned NAIC designations obtained after the SVO verifies compliance with the structural elements. As such, to ensure that nonconforming CTLs are not provided more favorable provisions than conforming CTLs that meet structural requirements, the Working Group confirmed that only CTLs that are filed with the NAIC SVO by February 15, 2021, shall be reported on Schedule D-1. Key aspects noted in this direction:

- a. This direction is a limited-time exception to the *NAIC Policy Statement on Coordination of the Accounting Practices and Procedures Manual and the Purposes and Procedures Manual of the Investment Analysis Office* and shall not be inferred to other investments. Pursuant to the noted Policy Statement, obtaining an NAIC designation does not change an investment’s applicable SSAP, annual or quarterly statement reporting schedule, or override other SSAP guidance required for the investment to be an admitted asset. Although nonconforming CTLs will be permitted to be

**INT 20-10**

- reported on Schedule D-1 when filed with the SVO for future receipt of an SVO-assigned NAIC designation (even without meeting structural requirements), this is strictly a limited-time exception to prevent reporting schedule changes while a larger project on the scope of Schedule D-1 is considered.
- b. The requirement to file the nonconforming CTL for an SVO-assigned NAIC designation for Schedule D-1 applies to all investments that represent credit tenant loans. It is not permissible for a reporting entity to classify an investment, which meets the characteristics of a credit tenant loan, as a different type of investment (for example, as a form of leased-backed security) for purposes of reporting the investment on Schedule D-1 without filing for an SVO-assigned NAIC designation.
  - c. The Working Group direction intends to only address nonconforming CTLs that have previously been reported on Schedule D-1 although they did not comply with the requirements of the P&P Manual. This direction is not intended to require, or permit, nonconforming CTLs that have been previously reported as mortgage loans (on Schedule B – Mortgage Loans) or as other invested assets (on Schedule BA – Other Long-Term Invested Assets) to be moved to a different reporting schedule. Nonconforming CTLs that have previously been reported on Schedule B or BA shall remain on that reporting schedule for the duration of this INT.

**INT 20-10 Consensus**

4. The Working Group reached a consensus to provide a limited time exception allowing nonconforming CTLs to continue to be reported on Schedule D-1 for year-end 2020 provided they have filed for an SVO-assigned NAIC designation. With the issuance of this interpretation, the Working Group confirmed the provisions and limitations detailed in paragraph 3, and summarized the resulting provisions below:
- a. CTLs that qualify per the provisions of the P&P Manual are considered to be “conforming” CTLs and shall be reported on Schedule D-1 with the NAIC designation obtained from the SVO.
  - b. CTLs that do not qualify per the provisions of the P&P Manual to be “conforming” CTLs shall follow the accounting and reporting provisions detailed in the following subparagraphs. These CTLs are noted as “nonconforming CTLs.”
    - i. Nonconforming CTLs that have previously been reported on Schedule D-1 may continue to be reported on Schedule D-1 for year-end 2020 if they have filed for an SVO-assigned NAIC designation. This provision only requires that an entity file the security with the SVO by February 15, 2021, not that the entity receive the SVO-assigned designation prior to submitting their 2020 annual statutory financial statements. If an entity does not file the security with the SVO by February 15, 2021, the investment shall be reported on Schedule BA. If reporting on Schedule BA, these CTLs shall not be reported with a credit-rating provider (CRP) determined NAIC designation. For nonconforming CTLs that have been filed with the SVO and retained on Schedule D-1, the reporting entity is required to disclose the total amount of nonconforming CTLs reported on Schedule D-1 on Note 1 as if it were a permitted practice. The reporting entity shall complete the permitted practice disclosures required by *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures*, with two separate entries that detail the nonconforming CTLs that were reported on D-1 on one line, and the nonconforming CTLs that were not reported on Schedule BA on a separate line within this disclosure. (These lines will likely net to a zero impact to statutory surplus; therefore, the separate line reporting is required.)



**INT 20-10**

- ii. Nonconforming CTLs that have been previously reported on a different reporting schedule (e.g., Schedule B or Schedule BA) shall remain on the prior reporting schedule. There is no requirement for reporting entities to pursue SVO-assigned designations for these CTLs or disclose these nonconforming CTLs in Note 1. Furthermore, reporting entities that have previously reported nonconforming CTLs on Schedule D-1 that do not want to file with the SVO or that do not want to disclose in Note 1 pursuant to paragraph 4.b.i. are permitted to reclassify these CTLs to Schedule B or Schedule BA without NAIC designations.

5. The exceptions granted in this interpretation are applicable for the year-end 2020 statutory financial statement only. Nonconforming CTLs that have been filed with the SVO and are reported on Schedule D-1 shall continue the Note 1 reporting for each 2021 quarterly financial statement until an SVO-assigned designation is received. The provisions within this INT, and the ability to continue reporting nonconforming CTLs on Schedule D-1 with an SVO-assigned NAIC designation, are limited time exceptions that extend only to October 1, 2021. The exceptions provided in this INT shall not be interpreted to indicate the likely conclusion of the Working Group in determining the appropriate reporting schedule for nonconforming CTLs. All reporting entities shall be prepared to make adjustments to comply with the reporting schedule utilized for nonconforming CTLs upon final conclusion by the Working Group.

**INT 20-10 Status**

6. On November 18, 2020, the Statutory Accounting Principles (E) Working Group exposed this interpretation to provide a limited-time exception on the reporting of nonconforming CTLs. On December 18, 2020, the Working Group exposed revisions to this interpretation to allow continued D-1 reporting of nonconforming CTLs if they are filed with the SVO by February 15, 2021. With this provision, nonconforming CTLs reported on Schedule D-1 that have not received an SVO-assigned designation shall be disclosed in Note 1 as if a permitted practice. On December 28, 2020, the Working Group finalized action, via evote, to adopt the interpretation exposed December 18, 2020.

7. No further discussion is planned.



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**MEMORANDUM**

**TO:** Kevin Fry, Chair, Valuation of Securities (E) Task Force  
Members of the Valuation of Securities (E) Task Force

**FROM:** Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)

**CC:** Marc Perlman, Investment Counsel, NAIC Securities Valuation Office (SVO)  
Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

**RE:** Proposed Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) to Update the List of NAIC CRPs

**DATE:** February 2, 2021

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- 1. Summary** – On July 2, 2019, Morningstar, Inc. completed its acquisition of DBRS. The merger was announced on May 29, 2019. DBRS Morningstar reported that they are now the fourth largest credit ratings agency and a market leader in Canada, the U.S. and Europe in multiple asset classes and rate more than 3,000 issuers and 60,000 securities worldwide. The merger resulted in the credit ratings symbols of the two previous entities being combined into a single set of symbols.
- 2. Recommendation** – The SVO recommend adoption of this non-substantive amendment removing references to the legacy entities and instead referring to the new combined national recognized statistical ratings organization (NRSRO) entity, DBRS, Inc., doing business as “DBRS Morningstar Credit Ratings” or “DBRS Morningstar.” This proposed change updates the rating agency names on the List of NAIC Credit Rating Providers to match those on the U.S. Securities and Exchange’s Office of Credit Ratings list of Current NRSROs and the CRP Credit Rating Equivalents to NAIC Designations and NAIC Designation Categories.
- 3. Proposed Amendment** – The text containing the updates to the List of NAIC CRPs is shown below, edits in red, as it would appear in the 2020 P&P Manual format.

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**PART THREE**  
**SVO PROCEDURES AND METHODOLOGY FOR PRODUCTION**  
**OF NAIC DESIGNATIONS**

**LIST OF NAIC CREDIT RATING PROVIDERS**

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22 The CRPs that provide Credit Rating Services to the NAIC are:

- **Moody's Investor's 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 Standard and Poor's**, 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.
- **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.
- ~~**Dominion Bond Rating Service (DBRS)** – 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.~~
- **A.M. Best Rating Services, Inc. Company (A.M. Best)** – For credit ratings issued to insurance companies; corporate issuers and issuers of asset-backed securities.
- ~~**Morningstar Credit Ratings, LLC** – For credit ratings issued to financial institutions, brokers, or dealers; 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.~~
- **Kroll Bond Rating Agency, 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.
- **Egan-Jones Ratings Co.mpany** – For credit ratings issued to financial institutions, brokers, or dealers; insurance companies and corporate issuers.

- **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.

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### CRP Credit Rating Equivalent to NAIC Designations and NAIC Designation Categories

~~23.~~ Please note that the existence of a rating does not eliminate the requirement to file on SAR on any insurer-owned security not currently listed in this Manual unless exempted from filing.

			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 Investor's Service, Inc.	S&P Global Ratings Standard and Poor's	Fitch Ratings, Inc.	DBRS, Inc. (DBRS)	A.M. Best Rating Services, Inc. Company	Morningstar Credit Ratings, LLC	Kroll Bond Rating Agency, Inc.	Egan Jones Rating Company	HR Ratings de Mexico, S.A. de C.V.	
1	A	1.A	Aaa	AAA	AAApr, AAA	AAA Pfd-1 (high)	aaa	AAA	AAA	AAA	HR AAA (G)	
1	B	1.B	Aa1	AA+	AA+	AA (high), Pfd-1	aa+	AA+	AA+	AA+	HR AA+ (G)	
1	C	1.C	Aa2	AA	AA	AA, Pfd-1 (low)	aa	AA	AA	AA	HR AA (G)	
1	D	1.D	Aa3	AA-	AA-	AA (low), Pfd-1	aa-	AA-	AA-	AA-	HR AA- (G)	
1	E	1.E	A1	A+	A+	A (high)	a+	A+	A+	A+	HR A+ (G)	
1	F	1.F	A2	A	A	A	a	A	A	A	HR A (G)	
1	G	1.G	A3	A-	A-	A (low)	a-	A-	A-	A-	HR A- (G)	
2	A	2.A	Baa1	BBB+	BBB+	BBB (high), Pfd-2 (high)	bbb+	BBB+	BBB+	BBB+	HR BBB+ (G)	
2	B	2.B	Baa2	BBB	BBB	BBB, Pfd-2	bbb	BBB	BBB	BBB	HR BBB (G)	
2	C	2.C	Baa3	BBB-	BBB-	BBB (low), Pfd-2 (low)	bbb-	BBB-	BBB-	BBB-	HR BBB- (G)	
3	A	3.A	Ba1	BB+	BB+	BB (high), Pfd-3 (high)	bb+	BB+	BB+	BB+	HR BB+ (G)	
3	B	3.B	Ba2	BB	BB	BB, Pfd-3	bb	BB	BB	BB	HR BB (G)	
3	C	3.C	Ba3	BB-	BB-	BB (low), Pfd-3 (low)	bb-	BB-	BB-	BB-	HR BB- (G)	
4	A	4.A	B1	B+	B+	B (high), Pfd-4 (high)	b+	B+	B+	B+	HR B+ (G)	
4	B	4.B	B2	B	B	B, Pfd-4	b	B	B	B	HR B (G)	
4	C	4.C	B3	B-	B-	B (low), Pfd-4 (low)	b-	B-	B-	B-	HR B- (G)	
5	A	5.A	Caa1	CCC+	CCC+	CCC (high), Pfd-5 (high)	ccc+	CCC+	CCC+	CCC+	HR C+ (G)	
5	B	5.B	Caa2	CCC	CCC	CCC, Pfd-5	ccc	CCC	CCC	CCC	HR C (G)	
5	C	5.C	Caa3	CCC-	CCC-	CCC (low), Pfd-5 (low)	ccc-	CCC-	CCC-	CCC-	HR C- (G)	
6	6	6	Ca	CC	CC	CC (high)	cc	CC	CC	CC	HR D (G)	
6	6	6	C	C	C	CC	c	C	C	C		
6	6	6		D	DDD	CC (low)	d	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 CRPs' 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 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")								
			Moody's Investor's Service, Inc.	S&P Global Ratings Standard and Poor's	Fitch Ratings, Inc.	DERS, Inc. (DERS Morningstar) Dominion Bond Rating Service	A.M. Best Rating Services, Inc. Company	Morningstar Credit Ratings, LLC	Kroll Bond Rating Agency, Inc.	Egan Jones Rating Company	HR Ratings de Mexico, S.A. de C.V.
NAIC Designation	NAIC Designation Modifier	NAIC Designation Category	Commercial Paper and Short Term Counterparty Ratings	Commercial Paper	Commercial Paper	Commercial Paper and Short Term Debt	Commercial Paper and Short Term Debt	N/A	Short-Term and Commercial Paper Ratings	Commercial Paper	N/A
1	A	1.A									
1	B	1.B									
1	C	1.C									
1	D	1.D	P1	A-1+	F1+	R1 (high)	AMB-1+		K1+	A1+	
1	E	1.E		A-1	F1	R-1 (middle)	AMB-1		K1	A1	
1	F	1.F				R-1 (low)				A	
2	A	2.A	P2	A-2	F2	R-2 (high)			K2	A2	
2	B	2.B				R-2 (middle)	AMB-2				
2	C	2.C	P3	A-3	F3	R-2 (low)				A3	
3	A	3.A									
3	B	3.B				R-3	AMB-3		K3		
3	C	3.C									
4	A	4.A									
4	B	4.B		B	B				B	B	
4	C	4.C									
5	A	5.A									
5	B	5.B	NP	C	C	R-4			C	C	
5	C	5.C									
6	6	6		SD	D	R-5	AMB-4		D	D	
6	6	6		D		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.

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