



NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Date: 11/17/2021

Virtual Meeting

Valuation of Securities (E) Task Force

Wednesday, November 17, 2021

1:00 – 2:00 p.m. ET / 12:00 – 1:00 p.m. CT / 11:00 – 12:00 p.m. MT / 10:00 – 11:00 a.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	Eric Dunning	Nebraska
Ricardo Lara	California	Marlene Caride	New Jersey
Andrew N. Mais	Connecticut	Russell Toal	New Mexico
Trinidad Navarro	Delaware	Adrienne A. Harris	New York
David Altmaier	Florida	Cassie Brown	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. Discuss and Consider Adoption of a Proposed Amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual) for the Addition of the United States International Development Finance Corporation (DFC) to the U.S. Government Full Faith and Credit – Filing Exempt List (Doc. ID: 2021-039.01 ID. 2021-039.02)
—Kevin Fry (IL), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment One & Attachment One - A

2. Discuss and Consider Adoption of a Proposed Amendment to the P&P Manual to Add Bank Loans (Doc. ID: 2021-041.01 ID. 2021-041-02)
—Kevin Fry (IL), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment Two & Attachment Two - A

3. Receive Referral from the Statutory Accounting Principles (E) Working Group and Consider Exposure of a Proposed Amendment to the P&P Manual to Remove Residuals Tranches from Receiving an NAIC Designation (Doc. ID: 2021-043.01 ID:2021-043.02 ID:2021-043.03)
—Kevin Fry (IL), Eric Kolchinsky (NAIC), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment Three & Three - A – Three - C



NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

4. Receive and Consider Exposure of a Proposed Technical Correction Amendment to the P&P Manual Clarifying 5GI Mapping to NAIC Designation Category (Doc. ID: 2021-044.01)
—Kevin Fry (IL), Charles Therriault (NAIC), Marc Perlman (NAIC) Attachment Four
5. Hear report from the Structured Securities Group on the Year-end Process
—Eric Kolchinsky (NAIC)
6. Any other matters

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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, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

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

RE: Addition of United States International Development Finance Corporation to the Purposes and Procedures Manual U.S. Government Full Faith and Credit – Filing Exempt List

DATE: September 3, 2021

Summary – An industry participant requested that the SVO add the U.S. International Development Finance Corporation to the “U.S. Government Full Faith and Credit – Filing Exempt” list in Part One of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (the “P&P”).

In October 2018 the Better Utilization of Investments Leading to Development (“BUILD”) Act was signed into law. The BUILD Act reorganized and merged existing United State government development finance and aid programs, the U.S. Overseas Private Investment Corporation (“OPIC”) and the Development Credit Authority of the United States Agency for International Development (“USAID”), into a new agency called the U.S. International Development Finance Corporation (“DFC”). The purpose of the DFC is to facilitate the participation of private sector capital and skills in the economic development of less developed countries and countries transitioning to market economies, while advancing U.S. foreign policy interests. It is authorized to do so by making loans or guaranties according to terms and conditions specified in the BUILD Act.

Pursuant to the BUILD Act, the support provided by the DFC shall, and existing support provided by OPIC and USAID shall continue, to constitute obligations of the United States, and the full faith and credit of the United States is thereby pledged for the full payment and performance of such obligations. The DFC is authorized to borrow from the U.S. Treasury to fulfill such obligations of the United States.

Based on this express full faith and credit, the SVO recommends adding the DFC to the “U.S. Government Full Faith and Credit – Filing Exempt” list in Part One of the P&P. We recommend maintaining OPIC and USAID on the list even though they have been subsumed by the DFC, because certain obligations of those agencies may still be outstanding.

For the avoidance of doubt, any security issued by an entity on the “U.S. Government Full Faith and Credit – Filing Exempt” list shall be filed with the SVO if the security is not *fully* guaranteed by the U.S. government. For certain entities on the list, statute may require parties other than the U.S. government

full faith and credit guarantor to bear a risk of loss equal to a specified percentage of the guaranteed support. For example, the BUILD Act requires parties to a project to bear the risk of loss in an amount of at least 20 percent of the guaranteed support of the DFC. If an insurance company, as investor, is the party bearing that risk of loss, meaning the securities it purchased are not fully guaranteed by the DFC or another entity on the list, it would need to file those securities with the SVO.

The P&P explains that the SVO has no compliance mechanism for these U.S. Government Obligations and encourages insurers which are uncertain about the Filing Exempt status of a security to either file it with the SVO or use the Regulatory Treatment Analysis Service (RTAS) – Emerging Investment Vehicle process. (P&P Part One, Paragraphs 75-76).

Proposed Amendment - The text changes to include the DFC on the “U.S. Government Full Faith and Credit – Filing Exempt” list is shown below with additions in red underline and deletions in ~~red strikethrough~~, as it would appear in the 2021 P&P Manual format.

PART ONE

POLICIES OF THE NAIC VALUATION OF SECURITIES (E) TASK FORCE

FILING EXEMPTION FOR U.S. GOVERNMENT SECURITIES
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Initial Filing Conventions and Documentation

66. **U.S. Government Securities Required to Be Filed with the SVO – U.S.**
Government debt that is not issued by, or guaranteed or insured by, those entities listed in below are subject to the filing exemption when rated by an NAIC CRP, otherwise, they must be filed with the SVO.

SVO Publishing Conventions for Filing Exempt U.S. Government Securities

67. **U.S. Treasury Obligations** – U.S. Treasury Obligations are added to the VOS Process automatically, and they appear in the VOS Product. The NAIC Designation is **NAIC 1** and the NAIC Designation Category is **NAIC 1.A**.

Other Filing Exempt U.S. Government Securities

68. A single entry is in the AVS+ Products in its normal CUSIP sequence, followed by the description “All Issues” for the securities listed below.
69. Because these securities are Filing Exempt, CUSIP numbers are not published in the AVS+ Products. The securities should, however, be reported with a CUSIP in the appropriate section of Schedule D. The NAIC Designation is **NAIC 1** and the NAIC Designation Category is **NAIC 1.A**.

Filing Requirements for U.S. Government Securities

70. No filing is required for the securities deemed exempt from filing below unless a state insurance department has specifically requested the SVO to evaluate an exempt security.
71. For U.S. Government Securities required to be filed with the SVO, the reporting insurance company shall submit:
- A prospectus of the security that includes a description of the U.S. government program under which it is issued; and
 - Appropriate evidence that the security or other obligation is backed by the U.S. government, an agency of the U.S. government or a U.S. government sponsored enterprise.
72. A variety of documents are acceptable as evidence that the issuer in question has some degree of support from the U.S. government. A copy of the legislation that created the entity or the program is acceptable as evidence of government support. Additionally, a copy of the guaranty or insurance policy for the transaction is also good evidence of government support. Another acceptable form of evidence is evidence of an NAIC CRP rating with a copy of the rating rationale memorandum discussing the role of U.S. government support. Oftentimes, the prospectus for the security describes in sufficient

detail the relationship of the entity to the U.S. government, its agency or its government-sponsored enterprise.

73. It is not enough to merely establish a relationship between the U.S. government and the entity. It is necessary to provide materials that specifically describe all of the financial terms of the obligation and the manner in which the U.S. government will pay the obligation.

Subsequent Filing

74. No subsequent report (i.e., an annual update filing) is required for non-exempt U.S. government securities. However, a material credit events filing is required for nonexempt U.S. government securities if:
- The legislation authorizing the program has been rescinded;
 - The transaction terms and/or the transaction documents have been waived, amended or modified; or
 - If the legal commitment of the U.S. government, U.S. government agency or U.S. government sponsored entity has been allowed to lapse or has been withdrawn.

Filing Exemption for Direct Claims on, or Backed by Full Faith and Credit of, the United States

75. This section defines what the NAIC deems to be U.S. Government Obligations. They are not required to be filed with the SVO.

NOTE: Because these filing exemption provisions are set forth without any compliance mechanism, the SVO will not be able to verify whether insurers have filed all securities that are required to be filed with the SVO. State insurance department regulators may wish to create their own compliance mechanisms to protect any interests they may have relative to their domiciliary insurers.

76. The SVO does not have responsibility for determining whether specific securities should be filing exempt. An insurer who is uncertain whether a specific security qualifies for exemption should not contact the SVO for guidance, but should either file the security with the SVO or use the RTAS – Emerging Investment Vehicle Service process and obtain an opinion on exemption for that security.

Definitions

77. **U.S. Government Obligation** – All direct claims (including securities, loans, and leases) on, and the portions of claims that are directly and unconditionally issued, guaranteed or insured by the U.S. Government or its agencies.
78. **U.S. Government Agency** – An instrumentality of the U.S. Government the debt

Obligations of which are fully guaranteed or insured as to the timely payment of principal and interest by the full faith and credit of the U.S. Government. This category includes in addition to direct claims on, and the portions of claims that are directly and unconditionally guaranteed by, the U.S. Government agencies listed below, claims collateralized by securities issued or guaranteed by the U.S. Government agencies listed below for which a positive margin of collateral is maintained on a daily basis, fully taking into account any change in the insurance company's exposure to the obligor or counterparty under a claim in relation to the market value of the collateral held in support of that claim.

U.S. Government Full Faith and Credit – Filing Exempt

Army and Air Force Exchange Service (AAFES)
Commodity Credit Corporation (CCC)
Export–Import Bank of the United States (EXIM Bank)
Farmers Home Administration (FmHA) – Certificates of Beneficial Ownership
Federal Deposit Insurance Corporation (FDIC)
Federal Housing Administration (FHA)
General Services Administration (GSA)
Government National Mortgage Association (GNMA)
National Credit Union Administration (NCUA)
Overseas Private Investment Corp (OPIC)
Small Business Administration (SBA)

U.S. Agency for International Development (USAID)
U.S. Department of Agriculture (USDA)
U.S. Department of Health and Human Services (HHS)
U.S. Department of Housing and Urban Development (HUD)
U.S. Department of the Treasury
U.S. Department of Veterans Affairs (VA)
[U.S. International Development Finance Corporation \(DFC\)](#)
U.S. Maritime Administration (MARAD)
Washington Metropolitan Area Transit Authority

Filing Exemption for Other U.S. Government Obligations

79. Obligations issued and either guaranteed or insured, as to the timely payment of principal and interest, by the government agencies or government-sponsored enterprises listed below are filing exempt. They are not backed by the full faith and credit of the U.S. Government. The filing exemption here is based on an analytical judgment that the combined creditworthiness of the entity itself and U.S. government support for that entity provides confidence that the issuer will be able to pay its obligation on a full and timely basis at the level of an **NAIC 1** quality designation and an NAIC Designation Category of **NAIC 1.A**. For the avoidance of doubt, preferred stock or similar securities of the government agencies or government-sponsored enterprises listed below are not considered guaranteed or insured and hence are not subject of this section.

**Filing Exempt Other U.S. Government Obligations
if issued and either fully guaranteed or insured by:**

Federal Agricultural Mortgage Corporation (Farmer Mac)
Federal Farm Credit Banks (FFCB)
Federal Financing Bank (FFB)
Federal Home Loan Banks (FHLB)
Federal Home Loan Mortgage Corporation (Freddie Mac)
Federal National Mortgage Association (Fannie Mae)
Financing Corporation (FICO)
Resolution Funding Corporation (REFCorp)
Tennessee Valley Authority (TVA)

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Amend PP To Add The DFC to US Gov List.docx



Michael Monahan
Senior Director, Accounting Policy
202-624-2324 t
mikemonahan@acli.com

October 29, 2021

Mr. Kevin Fry, Chairman Valuation
of Securities Task Force
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Exposure Draft to Add the United States International Development Finance Corporation (DFC) to the U.S. Government Full Faith and Credit – Filing Exempt List

Dear Mr. Fry:

The American Council of Life Insurers (ACLI) and the North American Securities Valuation Association (NASVA) (“the undersigned”) appreciate the opportunity to comment on the memo exposed after the September 30th, 2021, Valuation of Securities Task Force meeting regarding the addition of the “U.S. Government Full Faith and Credit – Filing Exempt List.”

The undersigned fully support the proposed criteria addition. We truly appreciate the constructive dialogue with you, the Task Force, and the Securities Valuation Office with this proposal.

We thank you for your continued engagement on the topic.

Sincerely,

A handwritten signature in black ink that reads 'M Monahan'.

M
Senior Director, Accounting Policy

Tracey Lindsey

Tracey Lindsey
NASVA

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

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 95 percent of industry assets in the United States.

acli.com

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ACLI_NASVA_CommentLettertoVOSTF_DFC_v102921.docx



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, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

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

RE: Addition of a Bank Loans section to the Purposes Procedures Manual of the NAIC Investment Analysis Office

DATE: September 3, 2021

Summary – Since 2018 the *Accounting Practices and Procedures Manual* has included bank loans issued directly by a reporting entity or acquired through a participation, syndication or assignment in *SSAP No. 26R – Bonds*. Pursuant to *SSAP No. 26R*, bank loans means fixed-income instruments, representing indebtedness of a borrower, made by a financial institution.

In order to maintain consistency with the bond definition in *SSAP No. 26R - Bonds*, the SVO proposes amending the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (the “P&P Manual”) to clarify that the SVO can assess and assign NAIC Designations to bank loans and the relevant filing instructions and methodology. The filing instructions and methodology would follow that of other corporate obligations.

Proposed Amendment - The text changes to add bank loans to the SVO’s credit assessment responsibilities is shown below with additions in red underline and deletions in ~~red-strikethrough~~, as it would appear in the 2021 P&P Manual format.

PART THREE

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

GENERAL CORPORATE AND MUNICIPAL METHODOLOGY FOR INDEPENDENT CREDIT QUALITY ASSESSMENT

NOTE: See “Special Instructions” (discussing Short-Term Investments, Circular Transactions, Mandatory Convertible Securities, Unrated Hybrid Securities and Sub-Paragraph D Companies) in Part One for policies that impact assignment of NAIC Designations.

27. Corporate bonds defined as the Obligations² of domestic and foreign corporations, and preferred stock shall be distinguished on the basis of the categories discussed below. The creditworthiness of the issuer of any particular category of Obligation shall be assessed by reference to the general, and any special, rating methodology discussed in this Part, unless the context of the analysis requires a different approach.

² **Obligation** means bonds, notes, debentures, certificates, including equipment trust certificates, production payments, bank certificates of deposit, bankers’ acceptances, credit tenant loans, loans secured by financing net leases, **bank loans made by a financial institution (issued directly by a reporting entity or acquired through a participation, syndication or assignment (each, as defined in SSAP No. 26R – Bonds))**, and other evidences of indebtedness for the payment of money (or a participation, certificates or other evidences of an interest in any of the foregoing), whether constituting general obligations of the issuer or payable only out of certain revenues or certain funds pledged or otherwise dedicated for payment.

BANK LOANS

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Michael Monahan
Senior Director, Accounting Policy
202-624-2324 t
mikemonahan@acli.com

October 29, 2021

Mr. Kevin Fry, Chairman Valuation
of Securities Task Force
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Exposure Draft to Add Bank Loans

Dear Mr. Fry:

The American Council of Life Insurers (ACLI) and the North American Securities Valuation Association (NASVA) (“the undersigned”) appreciate the opportunity to comment on the memo exposed after the September 30th, 2021, Valuation of Securities Task Force meeting regarding the addition of “Bank Loans.”

The undersigned fully support the proposed criteria addition. We truly appreciate the constructive dialogue with you, the Task Force, and the Securities Valuation Office with this proposal.

We thank you for your continued engagement on the topic.

Sincerely,

A handwritten signature in black ink, appearing to read 'M Monahan', is written in a cursive style.

Mike Monahan
Senior Director, Accounting Policy

Tracey Lindsey
NASVA

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

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 95 percent of industry assets in the United States.

acli.com



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, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

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

RE: Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (the "P&P Manual") to the clarify the exclusion of Residual Tranches and Interests from Schedule D-1 reporting and to provide temporary NAIC Designation instructions

DATE: November 1, 2021

Summary – The Statutory Accounting Principles (E) Working Group (the "Working Group") identified inconsistencies in how residual tranches and interests were being reported with some entities reporting them on Schedule BA – Other Long Term Invested Assets and others reporting them on Schedule D-1: Long-Term Bonds with either self-assigned NAIC 5GI or NAIC 6 Designations. To prevent further inconsistency and direct appropriate reporting, on September 9, 2021, the Working Group exposed an amendment to *SSAP 43R – Loan Backed and Structured Securities* to clarify that residual tranches and interests shall be report on Schedule BA. The Working Group plans to consider adoption of this amendment at their November 10, 2021, meeting.

The amendment creates a December 31, 2022 effective date for all residual tranches and interests to be reported on Schedule BA without an NAIC Designation. To accommodate the timeframe needed for Blanks (E) Working Group proposal 2021-21BWG to expand reporting lines on Schedule BA to capture residual tranches and interests, the Working Group's amendment permits residual tranches and interests currently reported on Schedule D-1 to continue to be reported on Schedule D-1 for reporting year 2021 but only with an NAIC 6* Designation and not an inappropriate NAIC 5GI Designation.

The NAIC 5GI Designation is not appropriate for residual tranches and interests (see definition from *SSAP 43R* below). Pursuant to the "P&P Manual, an insurance company is permitted to self-assign an NAIC 5GI to an obligation if it meets all of the following criteria:

1. Documentation necessary to permit a full credit analysis of the security by the SVO does not exist or an NAIC CRP rating for an FE or PL security is not available.
2. The issuer or obligor is current on all contracted interest and principal payments.
3. The insurer has an actual expectation of ultimate payment of all contracted interest and principal.

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Assignment of an NAIC 5GI Designation for residual investments is an incorrect application of the guidance as (a) there are no contracted interest and principal payments to certify as current and (b) the insurer cannot have an actual expectation of receiving all contractual principal and interest of the underlying collateral as these tranches absorb the losses first for the securitization structure. Although cash flows may pass through to the residual holders at periodic intervals pursuant to the waterfall, ultimate returns depend on continued performance so, therefore, there can be no actual expectation that future payments will be received.

The proposed amendment to *SSAP 43R – Loan Backed and Structured Securities* section 26.c., says:

For residual tranches or interests^{FN} captured in scope of this statement, all reporting entities (regardless of AVR) shall report the item on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value. Changes in the reported value from the prior period shall be recorded as unrealized gains or losses.

Footnote: Reference to “residual tranches or interests” intends to capture securitization tranches and beneficial interests as well as other structures captured in scope of this statement, that reflect loss layers without any contractual payments, whether principal or interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

The SVO recommends amendments to the P&P Manual to clarify the reporting requirements for residual tranches and interests in line with *SSAP 43R*, if and as amended.

Proposed Amendment - The text changes to include reporting instructions for residual tranches and interests is shown below with additions in red underline and deletions in ~~red strikethrough~~, as it would appear in the 2021 P&P Manual format. The SVO requests the Task Force’s permission to remove the paragraph with the “NOTE REGARDING RESIDUAL TRANCHES OR INTERESTS” from the December 31, 2022 version of the P&P Manual, without further authorization from the Task Force, as it will become obsolete at that time.

PART TWO

OPERATIONAL AND ADMINISTRATIVE INSTRUCTIONS APPLICABLE TO THE SVO

NAIC DESIGNATIONS RELATED TO SPECIAL REPORTING INSTRUCTIONS

27. An insurance company that self-assigns a 5GI must attest that securities receiving this designation meet all required qualifications by completing the appropriate general interrogatory in the statutory financial statements. If documentation necessary for the SVO to perform a full credit analysis for a security does not exist or if an NAIC CRP credit rating for an FE or PL security is not available, but the issuer is not current on contractual interest and principal payments, and/or if the insurer does not have an actual expectation of ultimate payment of all contracted interest and principal, the insurance company is required to self-assign this security an NAIC 6*.
28. NAIC 6* is assigned by an insurer to an obligation in lieu of reporting the obligation with appropriate documentation in instances in which appropriate documentation does not exist, but the requirements for an insurance company to assign a 5GI are not met.
29. Securities with NAIC 5GI Designations are deemed to possess the credit characteristics of securities assigned an NAIC 5 Designation. A security assigned an NAIC 5GI Designation incurs the regulatory treatment associated with an NAIC 5 Designation.
30. Securities an insurance company previously assigned as NAIC 5GI are permitted to subsequently receive this designation if the requirements for an NAIC 5GI designation continue to be met.
31. Securities with NAIC 6* Designations are deemed to possess the credit characteristics of securities assigned an NAIC 6 Designation. Therefore, a security assigned an NAIC 6* Designation incurs the regulatory treatment associated with an NAIC 6 Designation.
32. Securities that are residual tranches or interests, as defined in SSAP 43R – Loan Backed and Structured Securities, shall be reported on Schedule BA - Other Long-Term Invested Assets, without an NAIC Designation and are ineligible to be assigned an NAIC 5GI or NAIC 6* Designation.

NOTE REGARDING RESIDUAL TRANCHES OR INTERESTS: For 2021 year-end reporting only, residual tranches or interests previously reported on Schedule D-1: Long-Term Bonds shall be permitted to be reported on Schedule D-1 with an NAIC 6* Designation, however an NAIC 5GI is not permitted.

NOTE: The GI after the quality indicator 5 refers to General Interrogatory and distinguishes NAIC 5GI from an NAIC 5 Designation. The asterisk (*) after the quality indicator 6 distinguishes the NAIC 6* Designation from an NAIC 6 Designation.

PART THREE
SVO PROCEDURES AND METHODOLOGY FOR PRODUCTION
OF NAIC DESIGNATIONS

...

FE SECURITIES

Filing Exemption

3. Bonds, within the scope of SSAP No. 26R and SSAP No. 43R (excluding RMBS and CMBS subject to financial modeling) and Preferred Stock within scope of SSAP No. 32, that have been assigned an Eligible NAIC CRP Rating, as described in this Manual, are exempt from filing with the SVO (FE securities) with the exception of Bonds and/or Preferred Stock explicitly excluded below.

Specific Populations of Securities Not Eligible for Filing Exemption

4. The filing exemption procedure does not apply to:
 - ...
 - **Residual tranches or interests - As defined in SSAP 43R – Loan Backed and Structured Securities, residual tranches or interests shall be reported on Schedule BA - Other Long-Term Invested Assets, without an NAIC Designation and are therefore not eligible for filing exemption.**

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Hearing Agenda

**Statutory Accounting Principles (E) Working Group
Hearing Agenda
November 10, 2021
10:00 – 11:00 a.m. CT**

ROLL CALL

Dale Bruggeman, Chair	Ohio	Judy Weaver	Michigan
Carrie Mears/Kevin Clark, Co-Vice Chairs	Iowa	Doug Bartlett	New Hampshire
Sheila Travis	Alabama	Bob Kasinow	New York
Kim Hudson	California	Kimberly Rankin/Melissa Greiner	Pennsylvania
Kathy Belfi/William Arfanis	Connecticut	Jamie Walker	Texas
Rylynn Brown	Delaware	Doug Stolte/David Smith	Virginia
Eric Moser	Illinois	Amy Malm	Wisconsin
Stewart Guerin/Melissa Gibson	Louisiana		

NAIC Support Staff: Julie Gann, Robin Marcotte, Jim Pinegar, Jake Stultz, Jason Farr

REVIEW AND DISCUSSION - AGENDA ITEMS WITH DISCUSSION

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-15 SSAP No. 43R (Julie)	SSAP No. 43R – Residual Tranches	1 – Agenda Item	Comments Received	IP – 1

Summary:

On September 9, 2021, the Working Group exposed revisions to *SSAP No. 43R—Loan-Backed and Structured Securities* to clarify that non-rated residual tranches shall be reported on Schedule BA-Other Long-Term Invested Assets and valued at the lower of cost or fair value.

This agenda item was drafted due to identified inconsistencies for reporting residual tranches. From information received, some entities already report residual tranches on Schedule BA and other entities report these tranches on Schedule D-1: Long-Term Bonds with either a self-assigned 5GI or a self-assigned NAIC 6 designation. It has been noted that use of the NAIC 5GI process for these residual tranches is an incorrect application of the guidance as 1) there are no contractual interest and principal payments to certify as current, and 2) the insurer cannot have an actual expectation of receiving all contractual principal and interest of the underlying collateral as these tranches absorb the losses first for the securitization structure. Although cash flows may pass through to these holders at periodic intervals in a waterfall payment structure (a system in which the senior lenders/tranches receive principal and interest payments while other, subordinate lenders/tranches only receive principal and interest payments after the senior lenders/tranches have been paid), ultimate returns depend on continued performance, therefore, there can be no actual expectation that future payments will be received.

Interested Parties' Comments:

IPs have the following comments related to the proposal:

- 1) IPs agree that residual tranches or interests in scope of SSAP No. 43R, which meet the definition in the proposed footnote, should be reported on Schedule BA at lower of cost or market (“LOCOM”).

Hearing Agenda

Some companies already report such investments on Schedule BA and others report them on Schedule D measured at either LOCOM or amortized cost. We believe the proposed change in reporting would be cost justified as it would not be overly burdensome to insurers and would provide consistent reporting by insurers. It also would provide additional information for regulators to continue to evaluate such investments.

- 2) IPs believe an effective date of 12/31/2021 is achievable with regard to rating all residual tranches in the scope of SSAP No. 43R as NAIC 6. However, for various reasons noted below, IPs do not believe it would be feasible to transfer those residual tranches currently reported on Schedule D to Schedule BA for year-end 2021 reporting.

In conversations with NAIC staff and regulators, while working on the Working Group's Bond Project (formerly known as the 43R Project), IPs have been asked if adopting the proposal effective 12/31/2021 is feasible and also if reporting such interests on Schedule BA separately depending on the underlying collateral (e.g., fixed income, equity, real estate, etc.; same categories that currently exist on Schedule BA) would be feasible beginning at year-end 2022.

IPs believe that the 12/31/2021 reporting is not feasible as it would be operationally difficult to change processes in a timely manner prior to year-end reporting, including any vendor modifications that would be required, as well as address downstream implications such as impacts on cash flow statements and investment schedule rollforwards, etc., to ensure there are no unintended consequences related to the various statutory blanks and related processes. IPs support making such a change beginning at year-end 2022 and support the more granular reporting requested (i.e., based on underlying collateral) as it will allow the requisite amount of time to address those operational items discussed above. IPs also support allowing those companies that can address their processes prior to year-end 2021, the opportunity to transfer the residual tranches in scope from Schedule D to BA in 2021. It is important that the Working Group make companies aware that (1) the transfer of residual tranches to Schedule BA is optional for year-end 2021/quarterly 2022 and (2) if they choose to transfer the residual tranches to Schedule BA at year-end 2021, they would also be required to transfer them at year-end 2022 into the more granular categories discussed above based on underlying collateral (e.g., equities, fixed income, real estate, etc.). For those companies that decide to transfer the residual tranches in 2021, Blanks instructions would be needed well in advance of year-end to provide clarity related to the following:

- The specific section and subsection of Schedule BA where the residual tranches and interests in scope of this proposal would be reported.
 - How the various existing columns of Schedule BA would be used for such investments. For example, Schedule BA "cost" would be used to report "amortized cost" for such investments.
 - Communicating that LOCOM would be applied to such investments and clarifying where both amortized cost and fair value would be reported on the existing Schedule BA.
- 3) IPs recommend certain modifications to the proposed footnote and changes to SSAP No. 43R as follows:
 - Eliminate the reference to "non-rated" in paragraphs 26a, b, and c and the proposed footnote. IPs recommend eliminating the reference to non-rated as its definition may be interpreted inconsistently by various insurers (e.g., rated by the NAIC, rated by an NRSRO, insurer-rated such as NAIC 5 or 6?). We believe the intent is to exclude from Schedule D reporting, those investments that are typically not rated in the investment markets because their characteristics are not debt-like (e.g., no contractual payments of principal and/or interest) and thus we believe the inclusion of only the criteria "no contractual payments of principal and/or interest" will capture all investments intended to be captured.

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- IPs recommend removing the term “structured finance investments” from the footnote as it is an undefined term and is not clear to IPs as to what it is intended to capture. We believe retaining the references to “securitization tranches and beneficial interests” is adequate and would be understood to include all those investments intended by the regulators to be in the scope of the proposal.
- IPs recommend modifying the footnote to include those investments “...that reflect loss layers without contractual interest or principal payments” to those investments “...that reflect loss layers without any contractual payments, whether principal, interest, or both.” This proposed change would be more complete and “all-encompassing.”
- Ensure LOCOM is clarified to be “lower of **amortized cost** or market.” The use of the term “amortized cost” versus “cost” more accurately reflects the type of investment and is more aligned with the use of the term in existing SSAP No. 43R.

The following proposal reflects IPs comments discussed above as related to the footnote:

“Reference to “residual tranches or interests” intends to capture securitization tranches and beneficial interests as well as other structures captured in scope of this statement, that reflect loss layers without any contractual payments, whether principal, interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.”

Recommended Action:

NAIC staff recommends that the Working Group adopt the exposed revisions to SSAP No. 43R, modified to reflect the interested parties’ comments, as detailed below. Additionally, the revisions are proposed to have a December 31, 2022, effective date, with early application permitted. (This means that reporting entities can continue reporting on D-1 for 2021 but could reclassify to Schedule BA either to “Other” or another Schedule BA reporting line that is appropriate for the investment for year-end 2021.) The year-end 2022 effective date to require reporting on Schedule BA corresponds with blanks proposal 2021-21BWG. This blanks proposal expands the Schedule BA reporting lines to capture residual tranches based on underlying characteristics of fixed-income, common stock, real estate, mortgage loans and other. (These are the same categories used for items reported on Schedule BA in scope of SSAP No. 48—*Joint Ventures, Partnerships and Limited Liability Companies*.) (In addition to the IP edits, slight changes on the reference to AVR have been incorporated to mirror other instances in the SSAP.)

For residual tranches or interests retained on Schedule D-1 as of December 31, 2021, it is recommended that a joint memo from the Working Group and Valuation of Securities (E) Task Force be provided to the Blanks (E) Working Group to clarify that a self-assigned NAIC 5GI is not permitted for residual tranches, and such items reported on Schedule D-1 are required to be reported with an NAIC 6 designation. A referral to the Valuation of Securities (E) Task Force is recommended to support edits to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* to mitigate future misapplication of the NAIC 5GI process.

Proposed edits to the exposure reflect this recommendation along with the proposed interested parties’ edits are shown below:

Proposed edits to *SSAP No. 43R*:

(Revisions from the exposure shaded in gray.)

26. Loan-backed and structured securities shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and the

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designation assigned in the *NAIC Valuations of Securities* product prepared by the NAIC Securities Valuation Office or equivalent specified procedure. The carrying value method shall be determined as follows:

- a. For reporting entities that maintain an Asset Valuation Reserve (AVR), loan-backed and structured securities, excluding non-rated residual tranches or interests, shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value.
- b. For reporting entities that do not maintain an AVR, loan-backed and structured securities designated highest-quality and high-quality (NAIC designations 1 and 2, respectively), excluding non-rated residual tranches or interests, shall be reported at amortized cost; loan-backed and structured securities that are designated medium quality, low quality, lowest quality and in or near default (NAIC designations 3 to 6, respectively) shall be reported at the lower of amortized cost or fair value.
- c. For non-rated residual tranches or interests^{FN} captured in scope of this statement, all reporting entities (regardless of AVR) shall report the item on Schedule BA: Other Long-Term Invested Assets at the lower of amortized cost or fair value. Changes in the reported value from the prior period shall be recorded as unrealized gains or losses. For reporting entities that maintain an AVR, the accounting for unrealized gains and losses shall be in accordance with SSAP No. 7—Asset Valuation Reserve and Interest Maintenance Reserve.

New Footnote: Reference to “non-rated residual tranches or interests” intends to capture securitization tranches and beneficial interests, interests of structured finance investments, as well as other structures captured in scope of this statement, that reflect loss layers without any contractual payments, whether principal or interest, or both. interest or principal payments. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

Effective Date Guidance: *(The proposed subparagraph 56.h. below is new)*

56. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3—*Accounting Changes and Corrections of Errors*. Subsequent revisions to this statement include:
 - a. Substantive revisions pertaining to valuation and impairment based on expected cash flows, as detailed in *Issue Paper No. 140—Substantive Revisions to SSAP No. 43—Loan-Backed and Structured Securities*, were effective September 30, 2009. (Transition guidance previously included in SSAP No. 43R was removed from the SSAP in the *As of March 2018 Accounting Practices and Procedures Manual* but is retained for historical purposes in the issue paper.)
 - b. Substantive revisions to incorporate a new method to determine the final NAIC designation were effective, on a prospective basis, for reporting periods ending on or after December 31, 2009. In 2011, revisions were incorporated to this process to be consistent with the (P&P Manual). These revisions expanded the guidance to explicitly detail the process for “financial modeling” and “modified filing exempt” securities.
 - c. Nonsubstantive revisions to clarify the accounting for gains and losses between AVR and IMR securities were adopted in June 2010 with a January 1, 2011, effective date with early application allowed. Reporting entities that had previously bifurcated gains and losses between AVR and IMR

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- for sale transactions were restricted from reversing prior bifurcations and were prohibited from reverting to a process that did not bifurcate gains and losses in the period between adoption and the effective date.
- d. Nonsubstantive revisions, reflected in paragraph 50, to incorporate guidance from *INT 00-11: EITF 98-15: Structured Notes Acquired for a Specified Investment Strategy* were effective September 11, 2000.
 - e. Nonsubstantive revisions pertaining to the calculation of investment income for prepayment penalty and/or acceleration fees, reflected in paragraph 13, were effective January 1, 2017, on a prospective basis with early application permitted.
 - f. Nonsubstantive revisions to eliminate the modified filing exempt (MFE) method were effective March 31, 2019, with early adoption permitted for year-end 2018. Early adoption was considered an “all or nothing” approach. As such, reporting entities that did not elect to early adopt were required to apply the MFE process to all applicable SSAP No. 43R securities as of year-end 2018, whereas reporting entities that elected to early adopt were not permitted to use the MFE process for any SSAP No. 43R securities for year-end 2018.
 - g. Revisions adopted April 2019 to explicitly include mortgage-referenced securities in scope of this statement are effective December 31, 2019.
 - g.h. [Nonsubstantive revisions adopted in November 2021 to clarify that residual tranches or interests \(as defined in footnote \) shall be reported at the lower of amortized cost or fair value on Schedule BA: Other Invested Assets are effective December 31, 2022. Reporting entities may elect to reclassify residual tranches or interests to Schedule BA in advance of the effective date. As of the effective date, residual tranches or interests previously reported on Schedule BA shall be reclassified to the appropriate residual tranche Schedule BA reporting line based on the underlying characteristics of the investment structure.](#)

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-12EP Multiple (Robin)	Editorial Updates	2 – Agenda Item	No Comments	IP - 6

Summary:

On August 26, the Working Group exposed editorial revisions as summarized below:

- *Preamble* – Incorporates a paragraph number for the existing statutory hierarchy section.
- *Appendix A-001* - Updates designation codes for preferred stock as noted in section 2 of *Appendix A-001: Investments of Reporting Entities*.
- *Appendix C* - Updates reference to the *former* Emerging Actuarial Issues (E) Working Group as well as adding reference to the Valuation Analysis (E) Working Group’s use of included interpretations.
- *Appendix C-2* - Updates reference to the *former* Emerging Actuarial Issues (E) Working Group as well as adding reference to the Valuation Analysis (E) Working Group’s use of included interpretations.

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- *SSAP No. 21R—Other Admitted Assets* - Updates improve the readability of paragraph 9 regarding receivables for securities.

Interested Parties' Comments:

Interested parties have no comment on this item.

Recommended Action:

NAIC staff recommends that the Working Group adopt the editorial revisions to the Preamble, Appendix A-001, Appendix C, Appendix C-2 and SSAP No. 21R as final.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
2021-13 SSAP No. 55 (Robin)	Salvage – Legal Recoveries	3 – Agenda Item	Yes	IP - 6

Summary:

On August 26, the Working Group exposed revisions to *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* to clarify that subrogation recoveries should be reported as a reduction of losses and/or loss adjusting expense (LAE) reserves, depending on the nature of the costs being recovered. While this is believed to already be consistent with current practices of a majority of reporting entities, the revisions clarify that salvage and subrogation estimates and recoveries can include amounts related to both claims/losses and loss adjusting expenses (LAE). The corresponding estimates should be reported as a reduction of losses and/or LAE reserves, however once the amounts for salvage and subrogation and coordination of benefits (COB) are received, they shall be reported as a reduction of paid losses and LAE depending on the nature of the costs being recovered.

Interested Parties' Comments:

Interested parties support this proposal.

Recommended Action:

NAIC staff recommend that the Working Group adopt the exposed nonsubstantive revisions to *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*, which clarify that subrogation recoveries should be reported as a reduction of losses and/or loss adjusting expense reserves, depending on the nature of the costs being recovered. Included in this adoption is an updated to the related disclosures to reflect the reporting of estimated salvage and subrogation and their impact on unpaid claims, losses, or associated LAE.

Ref #	Title	Attachment #	Agreement with Exposed Document?	Comment Letter Page Number
INT 21-02T SSAP No. 6 (Jake)	Extension of Ninety-Day Rule for the Impact of Hurricane Ida	3 – Agenda Item	In Agreement	IP - 7

Summary:

On September 9 the Working Group exposed, via e-vote, a tentative interpretation (INT) to provide an optional 60-day extension from the “ninety-day rule” in *SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due from Agenda and Brokers* for related items that were directly impacted by Hurricane

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Ida. This INT is consistent with previous temporary extensions granted for other nationally significant catastrophes and is proposed to automatically nullify on January 24, 2022.

Interested Parties' Comments:

Interested parties support this proposal.

Recommended Action:

NAIC staff recommends adoption of the exposed INT. Due to the short-term nature of the applicability of this extension, which expires January 23, 2022, this interpretation will be publicly posted on the Statutory Accounting Principles (E) Working Group's website. Once the INT is nullified (on January 24, 2022) it will be included in *Appendix H – Superseded SSAPs and Nullified Interpretations in the As of March 2022 Accounting Practices and Procedures Manual.*

Note that the proposed extension temporarily overrides SSAP No. 6, paragraph 9, for affected policies; therefore, the policy statement in Appendix F (see authoritative literature) requires 2/3rd (two-thirds) of the Working Group members to be present and voting and a supermajority of the Working Group members present to vote in support of the interpretation before it can be finalized.

The comment letters are included as Attachment 5 (8 pages).

[https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2021/12.NovemberCall/00-8-26-21-SAPWG Hearing - 32R and 97.docx](https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2021/12.NovemberCall/00-8-26-21-SAPWG%20Hearing-32Rand97.docx)

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

Issue: SSAP No. 43R – Residual Tranches

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: Although the broad principles-based bond proposal project is establishing principles for reporting investments on Schedule D-1: Long-Term Bonds, it has been identified that there is current inconsistency in practice for the reporting of non-rated residual tranches for structures captured in scope of *SSAP No. 43R—Loan-Backed and Structured Securities*. To address this current inconsistency, it has been requested that revisions occur as an interim step to provide specific accounting and reporting for these items.

As background information, SSAP No. 43R provides guidance for investments in loan-backed and structured securities, as well as purchased and retained beneficial interests in securitized financial assets. The guidance presumes that the investments within scope reflect fixed-income instruments, particularly with the Schedule D-1: Long-Term Bond reporting as well as the amortized cost measurement method, but it has been identified that non-rated, first loss layers without contractual principal or interest (known as residual tranches or interests) are technically captured within the legal-form structure currently permitted within scope of the guidance.

As part of the principles-based bond project discussions, it has been identified that some entities report these residual investments on Schedule BA: Other Long-Term Investments. However, it has been noted that other entities report these residual tranches on Schedule D-1, as in scope of SSAP No. 43R. Since items on Schedule D-1 are required to have NAIC designations, and these tranches are not (and cannot be) rated from a CRP or receive an NAIC designation, some entities have applied the “NAIC 5GI” process to self-assign an NAIC 5 designation. For life entities, an NAIC 5 permits an amortized cost valuation and for all lines of business a NAIC 5 receives a lower RBC charge than what is received if reporting on Schedule BA.

The NAIC 5GI process permits entities to self-assign an NAIC 5 when they can certify to the following three components:

1. Documentation necessary to permit a full credit analysis of the security does not exist or an NAIC CRP ratings for an FE or PL security is not available.
2. The issuer or obligor is current on all contracted interest and principal payments.
3. The insurer has an actual expectation of ultimate payment of all contracted interest and principal payments.

Use of the NAIC 5GI process for non-rated residual investments is an incorrect application of the guidance as 1) there are no contracted interest and principal payments to certify as current and 2) the insurer cannot have an actual expectation of receiving all contractual principal and interest of the underlying collateral as these tranches absorb the losses first for the securitization structure. Although cash flows may pass through to these holders at periodic intervals in the waterfall, ultimate returns depend on continued performance, therefore, there can be no actual expectation that future payments will be received.

From the discussions that have occurred on the principles-based bond project, there is general agreement that these non-rated residual tranches do not belong on Schedule D-1 as long-term bonds. This agenda item proposes minor

revisions to SSAP No. 43R, as an interim action in advance of the adoption of the principles-based bond project, to prescribe the accounting and reporting for these non-rated residual investments to ensure consistent reporting. As detailed, it is proposed that these items remain in scope of SSAP No. 43R, as they are a component of a securitization, with specific guidance to report on Schedule BA with a lower of cost or fair value measurement.

Existing Authoritative Literature:

Reporting Guidance for All Loan-Backed and Structured Securities

26. Loan-backed and structured securities shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and the designation assigned in the *NAIC Valuations of Securities* product prepared by the NAIC Securities Valuation Office or equivalent specified procedure. The carrying value method shall be determined as follows:
- a. For reporting entities that maintain an Asset Valuation Reserve (AVR), loan-backed and structured securities shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value.
 - b. For reporting entities that do not maintain an AVR, loan-backed and structured securities designated highest-quality and high-quality (NAIC designations 1 and 2, respectively) shall be reported at amortized cost; loan-backed and structured securities that are designated medium quality, low quality, lowest quality and in or near default (NAIC designations 3 to 6, respectively) shall be reported at the lower of amortized cost or fair value.

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 Statutory Accounting Principles (E) Working Group has a comprehensive project to establish principles-based concepts for the definition for bond investments for reporting on Schedule D-1: Long-Term Bonds. This separate agenda item was directed as an interim action on Aug. 26, 2021, as it was identified that there is inconsistent reporting for non-rated residual tranches, with some entities reporting these non-rated loss-layer investments on D-1 with a self-assigned NAIC 5GI designation.

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

Convergence with International Financial Reporting Standards (IFRS): N/A

Staff Recommendation:

NAIC staff recommends that the Working Group move this item to the active listing, categorized as a new SAP concept, and expose revisions to SSAP No. 43R to establish specific accounting and reporting guidance for non-rated residual tranches or interests. Additionally, it is recommended that the Working Group sponsor a blanks proposal to capture a new reporting line specific for these items on Schedule BA and send a referral to the Valuation of Securities (E) Task Force to identify that the NAIC 5GI process shall not be used to self-assign an NAIC designation to non-rated residual investments.

Proposed edits to SSAP No. 43R:

Reporting Guidance for All Loan-Backed and Structured Securities

26. Loan-backed and structured securities shall be valued and reported in accordance with this statement, the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, and the designation assigned in the *NAIC Valuations of Securities* product prepared by the NAIC Securities Valuation Office or equivalent specified procedure. The carrying value method shall be determined as follows:

- a. For reporting entities that maintain an Asset Valuation Reserve (AVR), loan-backed and structured securities, excluding non-rated residual tranches or interests, shall be reported at amortized cost, except for those with an NAIC designation of 6, which shall be reported at the lower of amortized cost or fair value.
- b. For reporting entities that do not maintain an AVR, loan-backed and structured securities designated highest-quality and high-quality (NAIC designations 1 and 2, respectively), excluding non-rated residual tranches or interests, shall be reported at amortized cost; loan-backed and structured securities that are designated medium quality, low quality, lowest quality and in or near default (NAIC designations 3 to 6, respectively) shall be reported at the lower of amortized cost or fair value.
- c. For non-rated residual tranches or interests^{FN} captured in scope of this statement, all reporting entities (regardless of AVR) shall report the item on Schedule BA: Other Long-Term Invested Assets at the lower of cost or fair value. Changes in the reported value from the prior period shall be recorded as unrealized gains or losses.

New Footnote: Reference to “non-rated residual tranches or interests” intends to capture securitization tranches, beneficial interests, interests of structured finance investments, as well as other structures captured in scope of this statement, that reflect loss layers without contractual interest or principal payments. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

Staff Review Completed by: Julie Gann, NAIC Staff – September 2021

Status:

On September 9, 2021, in response to an e-vote to expose, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to *SSAP No. 43R—Loan-Backed and Structured Securities* to clarify that non-rated residual tranches shall be reported on Schedule BA – Other Long-Term Investments and valued at the lower of cost or fair value.

<https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2021/12.NovemberCall/1-21-15-SSAPNo.43R-ResidualTranches.docx>

NAIC Accounting Practices and Procedures Manual
Editorial and Maintenance Update
August 26, 2021

Maintenance updates provide revisions to the *Accounting Practices and Procedures Manual*, such as editorial corrections, reference changes and formatting.

SSAP/Appendix	Description/Revision
Preamble	Incorporates a paragraph number for the existing statutory hierarchy section.
Appendix A-001	Updates designation codes for preferred stock as noted in section 2 of <i>Appendix A-001: Investments of Reporting Entities</i> .
Appendix C	Updates reference to the <i>former</i> Emerging Actuarial Issues (E) Working Group as well as adding reference to the Valuation Analysis (E) Working Group's use of included interpretations.
Appendix C-2	Updates reference to the <i>former</i> Emerging Actuarial Issues (E) Working Group as well as adding reference to the Valuation Analysis (E) Working Group's use of included interpretations.
SSAP No. 21R	Updates improve the readability of paragraph 9 regarding receivables for securities.

Recommendation:

NAIC staff recommend that the Statutory Accounting Principles (E) Working Group move this agenda item to the active listing, categorize as nonsubstantive, and expose editorial revisions as illustrated below.

Status:

On August 26, 2021, the Statutory Accounting Principles (E) Working Group exposed the editorial revisions for comment.

Preamble

41. The multitude of unique circumstances and individual transactions makes it virtually impossible for any codification of accounting principles to be totally comprehensive. Application of SAP, either contained in the SSAPs or defined as GAAP and adopted by the NAIC, to unique circumstances or individual transactions should be consistent with the concepts of conservatism, consistency, and recognition.

V. Statutory Hierarchy

42. The following Hierarchy is not intended to preempt state legislative and regulatory authority.

Level 1

- SSAPs, including U.S. GAAP reference material to the extent adopted by the NAIC from the FASB Accounting Standards Codification¹ (FASB Codification or GAAP guidance)

Level 2

- Consensus positions of the Emerging Accounting Issues (E) Working Group as adopted by the NAIC (INTs adopted before 2016)

- Interpretations of existing SSAPs as adopted by the Statutory Accounting Principles (E) Working Group (INTs adopted in 2016 or beyond)

Level 3

- NAIC Annual Statement Instructions
- Purposes and Procedures Manual of the NAIC Investment Analysis Office

Level 4

- Statutory Accounting Principles Preamble and Statement of Concepts^[2]

Level 5

- Sources of nonauthoritative GAAP accounting guidance and literature, including: (a) practices that are widely recognized and prevalent either generally or in the industry, (b) FASB Concept Statements, (c) AICPA guidance not included in FASB Codification, (d) International Financial Reporting Standards, (e) Pronouncements of professional associations or regulatory agencies, (f) Technical Information Service Inquiries and Replies included in the AICPA Technical Practice Aids, and (g) Accounting textbooks, handbooks and articles

432. If the accounting treatment of a transaction or event is not specified by the SSAPs, preparers, regulators and auditors of statutory financial statements should consider whether the accounting treatment is specified by another source of established statutory accounting principles. If an established statutory accounting principle from one or more sources in Level 2 or 3 is relevant to the circumstances, the preparer, regulator or auditor should apply such principle. If there is a conflict between statutory accounting principles from one or more sources in Level 2 or 3, the preparer, regulator or auditor should follow the treatment specified by the source in the higher level—that is, follow Level 2 treatment over Level 3. Revisions to guidance in accordance with additions or revisions to the NAIC statutory hierarchy should be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*.

^[1] Effective September 15, 2009, the FASB Codification is the source of authoritative U.S. generally accepted accounting principles. As of that date, the FASB Codification superseded all then-existing non-SEC accounting and reporting standards. All other nongrandfathered, non-SEC accounting literature not included in the FASB Codification is nonauthoritative. As of September 15, 2009, AICPA Statements of Position are no longer reviewed as part of the statutory maintenance process as they are no longer considered authoritative GAAP literature. If the AICPA were to address an issue that affects the FASB Codification, an accounting standard update (ASU) would be issued and reviewed for applicability to statutory accounting.

^[2] The Statutory Accounting Principles Statement of Concepts incorporates by reference FASB Concepts Statements One, Two, Five and Six to the extent they do not conflict with the concepts outlined in the statement. However, for purposes of applying this hierarchy the FASB Concepts Statements shall be included in Level 5 and only those concepts unique to statutory accounting as stated in the statement are included in Level 4.

Appendix A-001 Investments of Reporting Entities

Update designation codes for preferred stock – the codes marked for deletion are no longer in use. Note: the blanks have already been updated through an editorial update that occurred in March 2021.

Section 2. Investment Risks Interrogatories

3. Amounts and percentages of the reporting entity’s total admitted assets held in bonds and preferred stocks by NAIC designation:

	Bonds				Preferred Stocks			
		<u>1</u>	<u>2</u>			<u>3</u>	<u>4</u>	
3.01	NAIC – 1	\$ .....	.....%	3.07	NAIC P/RP – 1	\$ .....	.....	%
3.02	NAIC – 2	\$ .....	.....%	3.08	NAIC P/RP – 2	\$ .....	.....	%
3.03	NAIC – 3	\$ .....	.....%	3.09	NAIC P/RP – 3	\$ .....	.....	%

3.04	NAIC – 4	\$ .....	.....%	3.10	NAIC P/RP – 4	\$ %
3.05	NAIC – 5	\$ .....	.....%	3.11	NAIC P/RP – 5	\$ %
3.06	NAIC – 6	\$ .....	.....%	3.12	NAIC P/RP – 6	\$ %

Appendix C Actuarial Guidelines - Appendices

Updates reference to the *former* Emerging Actuarial Issues (E) Working Group as well as adding reference the Valuation Analysis (E) Working Group’s use of included interpretations.

Includes interpretations from the [former](#) Emerging Actuarial Issues (E) Working Group adopted by the Financial Condition (E) Committee. The Financial Analysis (E) Working Group [and the Valuation Analysis \(E\) Working Group](#) follows these interpretations [in when](#) performing ~~its~~ reviews of the reserving methodologies under *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38).

Appendix C-2 Interpretations of the Emerging Actuarial Issues (E) Working Group

Updates reference to the *former* Emerging Actuarial Issues (E) Working Group as well as adding reference the Valuation Analysis (E) Working Group’s use of included interpretations.

Introduction

The [former](#) Emerging Actuarial Issues (E) Working Group ([EAIWG](#)) and the current [Valuation Analysis \(E\) Working Group \(VAWG\)](#) responds to questions of application, interpretation and clarification with respect to *Actuarial Guideline XXXVIII—The Application of the Valuation of Life Insurance Policies Model Regulation* (AG 38). Following an abbreviated public comment and review period of no less than seven days, the Working Group will adopt by consensus formal interpretations on issues presented before it. These interpretations will then be reported to the Financial Condition (E) Committee, which, after adopting, will direct the Financial Analysis (E) Working Group to follow the interpretations in performing its reviews of the reserving methodologies under AG 38. These interpretations will not become effective until formally adopted by the Financial Condition (E) Committee. In no event shall a consensus opinion of the [former EAIWG Working Group or current VAWG](#) supersede or otherwise conflict with AG 38.

SSAP No. 21R—Other Admitted Assets

Updates improve the readability of paragraph 9 regarding receivables for securities.

9. Sales of securities are recorded as of the trade date. A receivable due from the broker is established in instances when a security has been sold, but the proceeds from the sale have not yet been received. Unless the receivable for securities, [meets the criteria set forth in paragraph 11, the receivable for securities is an admitted asset to the extent it conforms to the requirements of this statement. For other than a receivables](#) arising from the sale of a security which was acquired on a “To Be Announced” (“TBA”) basis, or from the sale of securities that are received as stock distributions that may be restricted (unregistered) or in physical form, and which has yet to be actually received, [admissibility shall be in accordance with \(see paragraph 12.\); meets the criteria set forth in paragraph 11, the receivable for securities is an admitted asset to the extent it conforms to the requirements of this statement.](#)

Status:

On August 26, 2021, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed editorial revisions to the Preamble, *Appendix A-001: Investments of Reporting Entities, Appendix C Actuarial Guidelines – Appendices, Appendix C-2 Interpretations of the Emerging Actuarial Issues (E) Working Group, and SSAP No. 21R —Other Admitted Assets, as illustrated above.*

<https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/National Meetings/A. National Meeting Materials/2021/12. November Call/2 - 21-12EP August 2021.docx>

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

Issue: Salvage - Legal Recoveries

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 recommends nonsubstantive revisions to *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* to clarify that salvage and subrogation estimates and recoveries can include amounts related to both claims/ losses and loss adjusting expenses. The corresponding estimates should be reported as a reduction of losses and/or loss adjusting expense (LAE) reserves. Once the amounts for salvage and subrogation and coordination of benefits recoveries (COB) are received, they are reported as a reduction of paid losses and LAE depending on the nature of the costs being recovered.

SSAP No. 55 contains salvage and subrogation guidance. Key points of the guidance regarding salvage, subrogation and COB are as follows:

- Salvage, subrogation and coordination of benefits recoveries are estimated using the same techniques used for estimating unpaid claims/losses and unpaid loss adjusting expenses.
- Separate recoverables are not established. Estimated salvage, subrogation and coordination of benefit recoveries (net of associated expenses) are deducted from the liability for unpaid claims or losses (for reporting entities that choose to anticipate such recoveries).
- Salvage, subrogation and coordination of benefits recoveries received (net of associated expenses) are reported as a reduction to paid losses/claims.

This agenda item is in response to an industry request. The proposed clarification provides additional detail regarding loss adjusting expenses for salvage, subrogation and coordination of benefits that is believed to be consistent with current practice by a majority of reporting entities. For example, if legal fees are recovered in a subrogation lawsuit, it is believed that such amounts are currently being reported as reduction in paid adjusting expenses for legal fees. SSAP No. 55 does not explicitly discuss the recovery of loss adjusting expenses in the discussion of salvage, subrogation and COB. However, the property and casualty annual statement instructions, which are level two on the statutory hierarchy of authoritative literature, includes an explicit reference to reduce loss adjusting expenses for such amounts in the Schedule P instructions (See Existing Authoritative Literature below).

Existing Authoritative Literature:

SSAP No. 55 provides the following (bolding added for emphasis):

General

11. The liability for claim reserves and claim liabilities, unpaid losses, and loss/claim adjustment expenses shall be based upon the estimated ultimate cost of settling the claims (including the effects of inflation and other societal and economic factors), using past experience adjusted for current trends, and any other factors that would modify past experience. These liabilities shall not be discounted unless authorized for specific types of claims by specific SSAPs, including SSAP No. 54R and *SSAP No. 65—Property and Casualty Contracts*.

12. Various analytical techniques can be used to estimate the liability for IBNR claims, future development on reported losses/claims, and loss/claim adjustment expenses. These techniques generally consist of statistical analysis of historical experience and are commonly referred to as loss reserve projections. The estimation process is generally performed by line of business, grouping contracts with like characteristics and policy provisions. The decision to use a particular projection method and the results obtained from that method shall be evaluated by considering the inherent assumptions underlying the method and the appropriateness of those assumptions to the circumstances. No single projection method is inherently better than any other in all circumstances. The results of more than one method should be considered.

13. For each line of business and for all lines of business in the aggregate, management shall record its best estimate of its liabilities for unpaid claims, unpaid losses, and loss/claim adjustment expenses. Because the ultimate settlement of claims (including IBNR for death claims and accident and health claims) is subject to future events, no single claim or loss and loss/claim adjustment expense reserve can be considered accurate with certainty. Management's analysis of the reasonableness of claim or loss and loss/claim adjustment expense reserve estimates shall include an analysis of the amount of variability in the estimate. If, for a particular line of business, management develops its estimate considering a range of claim or loss and loss/claim adjustment expense reserve estimates bounded by a high and a low estimate, management's best estimate of the liability within that range shall be recorded. The high and low ends of the range shall not correspond to an absolute best-and-worst case scenario of ultimate settlements because such estimates may be the result of unlikely assumptions. Management's range shall be realistic and, therefore, shall not include the set of all possible outcomes but only those outcomes that are considered reasonable. Management shall also follow the concept of conservatism included in the Preamble when determining estimates for claims reserves. However, there is not a specific requirement to include a provision for adverse deviation in claims.

14. In the rare instances when, for a particular line of business, after considering the relative probability of the points within management's estimated range, it is determined that no point within management's estimate of the range is a better estimate than any other point, the midpoint within management's estimate of the range shall be accrued. It is anticipated that using the midpoint in a range will be applicable only when there is a continuous range of possible values, and no amount within that range is any more probable than any other. For purposes of this statement, it is assumed that management can quantify the high end of the range. If management determines that the high end of the range cannot be quantified, then a range does not exist, and management's best estimate shall be accrued. This guidance is not applicable when there are several point estimates which have been determined as equally possible values, but those point estimates do not constitute a range. If there are several point estimates with equal probabilities, management should determine its best estimate of the liability.

15. If a reporting entity chooses to anticipate salvage and subrogation recoverables (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), the recoverables shall be estimated in a manner consistent with paragraphs 11-13 of this statement. Estimated salvage and subrogation recoveries (net of associated expenses) shall be deducted from the liability for unpaid claims or losses. If a reporting entity chooses to anticipate coordination of benefits (COB) recoverables of Individual and Group Accident and Health Contracts, the recoverables shall be estimated in a manner consistent with paragraphs 11-13 of this statement and shall be deducted from the liability for unpaid claims or losses. A separate receivable shall not be established for these recoverables. In addition, all of these recoverables are also subject to the impairment guidelines established in SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets and an entity shall not reduce its reserves for any recoverables deemed to be impaired. Salvage and subrogation recoveries received (net of associated expenses) are reported as a reduction to paid losses/claims. Coordination of benefits (COB) recoveries received of Individual and Group Accident and Health Contracts (net of associated expenses) are reported as a reduction to paid claims.

16. Changes in estimates of the liabilities for unpaid claims or losses and loss/claim adjustment expenses resulting from the continuous review process, including the consideration of differences between estimated and actual payments, shall be considered a change in estimate and shall be recorded in accordance with SSAP No. 3—Accounting Changes and Corrections of Errors. SSAP No. 3 requires

changes in estimates to be included in the statement of operations in the period the change becomes known. This guidance also applies to the period subsequent to the March 1 filing deadline for annual financial statements through the filing deadline of June 1 for audited annual financial statements.

Disclosures

17. The financial statements shall include the following disclosures for each year full financial statements are presented. The disclosure requirement in paragraph 17.d. is also applicable to the interim financial statements if there is a material change from the amounts reported in the annual filing. Life and annuity contracts are not subject to this disclosure requirement.

- a. The balance in the liabilities for unpaid claims and unpaid losses and loss/claim adjustment expense reserves at the beginning and end of each year presented;
- b. Incurred claims, losses, and loss/claim adjustment expenses with separate disclosures of the provision for insured or covered events of the current year and increases or decreases in the provision for insured or covered events of prior years;
- c. Payments of claims, losses, and loss/claim adjustment expenses with separate disclosures of payments of losses and loss/claim adjustment expenses attributable to insured or covered events of the current year and insured or covered events of prior years;
- d. The reasons for the change in the provision for incurred claims, losses, and loss/claim adjustment expenses attributable to insured or covered events of prior years. The disclosure should indicate whether additional premiums or return premiums have been accrued as a result of the prior-year effects. (For Title reporting entities, "provision" refers to the known claims reserve included in Line 1 of the Liabilities page, and "prior years" refers to prior report years);
- e. Information about significant changes in methodologies and assumptions used in calculating the liability for unpaid claims and claim adjustment expenses, including reasons for the change and the effects on the financial statements for the most recent reporting period presented;
- f. A summary of management's policies and methodologies for estimating the liabilities for losses and loss/claim adjustment expenses, including discussion of claims for toxic waste cleanup, asbestos-related illnesses, or other environmental remediation exposures;
- g. Disclosure of the amount paid and reserved for losses and loss/claim adjustment expenses for asbestos and/or environmental claims, on a direct, assumed and net of reinsurance basis (the reserves required to be disclosed in this section shall exclude amounts relating to policies specifically written to cover asbestos and environmental exposures). Each company should report only its share of a group amount (after applying its respective pooling percentage) if the company is a member of an intercompany pooling agreement; and
- h. **Estimates of anticipated salvage and subrogation (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), deducted from the liability for unpaid claims or losses.**

The Property and Casualty Annual Statement Instructions for Schedule P, Part 1 discuss salvage and subrogation regarding loss reserve and paid claims and **then provide additional detail regarding losses and loss adjusting expenses in a later paragraph as excerpted below (bolding added for emphasis);**

Cumulative salvage and subrogation received and losses and expenses paid should be reported for each specific year. For "prior," report only salvage and subrogation received and losses and expenses paid in current year.

In Schedule P, Part 1, salvage and subrogation received should be reported net of reinsurance, if any. Loss payments are to be reported net of salvage and subrogation received in Schedule P.

Adjusting & Other Payments, Column 9, should only reflect ceded recoveries made in 1997 and subsequent. Adjusting & Other Payments, Column 8, should reflect net payments in 1996 and prior and direct and assumed payments for 1997 and subsequent.

Premiums earned and losses paid, unpaid, and incurred should reconcile with the Statement of Income page. The workpapers that show a reconciliation explaining reinsurance, discounting, and salvage and subrogation adjustments should be available for examination on request.

Report in Column 23 the estimated amount of anticipated salvage and subrogation that has been taken as credit (netted) in the reserves for **unpaid losses and loss adjustment expenses** reported in Column 24. (Note: Column 23 is a memo column only as the amounts contained therein have already been taken into consideration in Columns 13 through 20.)

The Life and Health Annual Statement Instructions for Note 36 (matches SSAP No. 55, paragraph 17h disclosure.)

36. Loss/Claim Adjustment Expenses

Instruction:

The financial statement shall include the following disclosures for each year full financial statements are presented. Life and annuity contracts are not subject to this disclosure requirement:

- The balance in the liabilities for unpaid loss/claim adjustment expense reserves at the beginning and end of each year presented.
- Incurred loss/claim adjustment expenses with separate disclosures of the provision for insured or covered events of the current year and increases or decreases in the provision for insured or covered events of prior years.
- Payments of loss/claim adjustment expenses with separate disclosure of payment of loss/claim adjustment expenses attributable to insured or covered events of the current year and insured or covered events of prior years.
- **Estimates of anticipated salvage and subrogation (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), deducted from the liability for unpaid claims or losses.**

Illustration:

The balance in the **liability for unpaid accident and health claim adjustment expenses** as of and _____ was \$ _____ and \$ _____, respectively.

The Company incurred \$ _____ and paid \$ _____ of **claim adjustment expenses** in the current year, of which \$ _____ of the paid amount was attributable to insured or covered events of prior years. The Company did not increase or decrease the provision for insured events of prior years.

The Company took into account estimated anticipated salvage and subrogation of the liability for unpaid claims/losses and reduced such liability by \$ _____.

The Health Annual Statement Instructions for note 31 matches SSAP No. 55, paragraph 17h disclosure.

31. Anticipated Salvage and Subrogation

Instruction:

Estimates of anticipated salvage and subrogation (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), deducted from the liability for unpaid claims or losses. Refer to SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses for accounting guidance.

Illustration:

The Company took into account estimated anticipated salvage and subrogation in its determination of the liability for unpaid claims/losses and reduced such liability by \$_____.

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): None

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 Review Completed by:

Robin Marcotte - NAIC Staff, August 2021

Staff Recommendation:

NAIC staff recommends that the Working Group move this agenda item to the active listing, categorized as nonsubstantive, and expose revisions to SSAP No. 55, which clarify that subrogation recoveries should be reported as a reduction of losses and/or loss adjusting expense LAE reserves, depending on the nature of the costs being recovered. In addition, updates to the disclosure in paragraph 17h are recommended. In conjunction, with the agenda item, NAIC staff should be directed to coordinate develop conforming revisions to the annual statement instructions. While NAIC staff believes the proposed clarification is consistent with the current practice of most entities, the Working Group should notify the Casualty Actuarial and Statistical (C) Task Force, the Life Actuarial (A) Task Force and the Health Actuarial (B) Task Force of the exposure.

SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses proposed revisions

General

11. The liability for claim reserves and claim liabilities, unpaid losses, and loss/claim adjustment expenses shall be based upon the estimated ultimate cost of settling the claims (including the effects of inflation and other societal and economic factors), using past experience adjusted for current trends, and any other factors that would modify past experience. These liabilities shall not be discounted unless authorized for specific types of claims by specific SSAPs, including SSAP No. 54R and SSAP No. 65—Property and Casualty Contracts.

12. Various analytical techniques can be used to estimate the liability for IBNR claims, future development on reported losses/claims, and loss/claim adjustment expenses. These techniques generally consist of statistical analysis of historical experience and are commonly referred to as loss reserve projections. The estimation process is generally performed by line of business, grouping contracts with like characteristics and policy provisions. The decision to use a particular projection method and the results obtained from that method shall be evaluated by considering the inherent assumptions underlying the method and the appropriateness of those assumptions to the circumstances. No single projection method

is inherently better than any other in all circumstances. The results of more than one method should be considered.

13. For each line of business and for all lines of business in the aggregate, management shall record its best estimate of its liabilities for unpaid claims, unpaid losses, and loss/claim adjustment expenses. Because the ultimate settlement of claims (including IBNR for death claims and accident and health claims) is subject to future events, no single claim or loss and loss/claim adjustment expense reserve can be considered accurate with certainty. Management's analysis of the reasonableness of claim or loss and loss/claim adjustment expense reserve estimates shall include an analysis of the amount of variability in the estimate. If, for a particular line of business, management develops its estimate considering a range of claim or loss and loss/claim adjustment expense reserve estimates bounded by a high and a low estimate, management's best estimate of the liability within that range shall be recorded. The high and low ends of the range shall not correspond to an absolute best-and-worst case scenario of ultimate settlements because such estimates may be the result of unlikely assumptions. Management's range shall be realistic and therefore, shall not include the set of all possible outcomes but only those outcomes that are considered reasonable. Management shall also follow the concept of conservatism included in the Preamble when determining estimates for ~~claims~~ claim and loss and loss/claim adjustment expense reserves. However, there is not a specific requirement to include a provision for adverse deviation in claims.

14. In the rare instances when, for a particular line of business, after considering the relative probability of the points within management's estimated range, it is determined that no point within management's estimate of the range is a better estimate than any other point, the midpoint within management's estimate of the range shall be accrued. It is anticipated that using the midpoint in a range will be applicable only when there is a continuous range of possible values, and no amount within that range is any more probable than any other. For purposes of this statement, it is assumed that management can quantify the high end of the range. If management determines that the high end of the range cannot be quantified, then a range does not exist, and management's best estimate shall be accrued. This guidance is not applicable when there are several point estimates which have been determined as equally possible values, but those point estimates do not constitute a range. If there are several point estimates with equal probabilities, management should determine its best estimate of the liability.

15. If a reporting entity chooses to anticipate salvage and subrogation recoverables (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), the recoverables shall be estimated in a manner consistent with paragraphs 10-12 of this statement. Estimated salvage and subrogation recoveries (net of associated recovery expenses) shall be deducted from the liability for unpaid claims, unpaid losses, and unpaid loss/claim adjustment expenses, depending on the whether the subrogation represents a recovery of claims/losses or loss/claims adjustment expenses-or-losses. If a reporting entity chooses to anticipate coordination of benefits (COB) recoverables of Individual and Group Accident and Health Contracts, the recoverables shall be estimated in a manner consistent with paragraphs 11-13 of this statement and shall be deducted from the liability for unpaid claims or losses. A separate receivable shall not be established for these recoverables. In addition, all of these recoverables are also subject to the impairment guidelines established in *SSAP No. 5R—Liabilities, Contingencies and Impairments of Assets* (SSAP No. 5R) and an entity shall not reduce its reserves for any recoverables deemed to be impaired. Salvage and subrogation recoveries received (net of associated recovery expenses) are reported as a reduction to paid losses/claims and/or paid loss/claim adjustment expenses. Coordination of benefits (COB) recoveries received of Individual and Group Accident and Health Contracts (net of associated recovery expenses) are reported as a reduction to paid claims.

Disclosures

17. The financial statements shall include the following disclosures for each year full financial statements are presented. The disclosure requirement in paragraph 17.d. is also applicable to the interim financial statements if there is a material change from the amounts reported in the annual filing. Life and annuity contracts are not subject to this disclosure requirement.

- a. The balance in the liabilities for unpaid claims and unpaid losses and loss/claim adjustment expense reserves at the beginning and end of each year presented;

- b. Incurred claims, losses, and loss/claim adjustment expenses with separate disclosures of the provision for insured or covered events of the current year and increases or decreases in the provision for insured or covered events of prior years;
- c. Payments of claims, losses, and loss/claim adjustment expenses with separate disclosures of payments of losses and loss/claim adjustment expenses attributable to insured or covered events of the current year and insured or covered events of prior years;
- d. The reasons for the change in the provision for incurred claims, losses, and loss/claim adjustment expenses attributable to insured or covered events of prior years. The disclosure should indicate whether additional premiums or return premiums have been accrued as a result of the prior-year effects. (For Title reporting entities, “provision” refers to the known claims reserve included in Line 1 of the Liabilities page, and “prior years” refers to prior report years);
- e. Information about significant changes in methodologies and assumptions used in calculating the liability for unpaid claims and claim adjustment expenses, including reasons for the change and the effects on the financial statements for the most recent reporting period presented;
- f. A summary of management’s policies and methodologies for estimating the liabilities for losses and loss/claim adjustment expenses, including discussion of claims for toxic waste cleanup, asbestos-related illnesses, or other environmental remediation exposures;
- g. Disclosure of the amount paid and reserved for losses and loss/claim adjustment expenses for asbestos and/or environmental claims, on a direct, assumed and net of reinsurance basis (the reserves required to be disclosed in this section shall exclude amounts relating to policies specifically written to cover asbestos and environmental exposures). Each company should report only its share of a group amount (after applying its respective pooling percentage) if the company is a member of an intercompany pooling agreement; and
- h. Estimates of anticipated salvage and subrogation (including amounts recoverable from second injury funds, other governmental agencies, or quasi-governmental agencies, where applicable), deducted from the liability for unpaid claims, ~~or~~ losses or their associated adjusting expenses.

Status:

On August 26, 2021, the Statutory Accounting Principles (E) Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and took the following actions:

1. Exposed revisions to *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*, as illustrated above, to clarify that salvage and subrogation recoveries should be reported as a reduction of losses and/or loss adjusting expense (LAE reserves), depending on the nature of the costs being recovered. In addition, updates to the disclosure in paragraph 17.h. were exposed.
2. Directed NAIC staff to coordinate develop conforming revisions to the Annual Statement instructions.
3. Directed notification of the exposure to the following actuarial Task Forces:
 - a. Casualty Actuarial and Statistical (C) Task Force,
 - b. Life Actuarial (A) Task Force, and
 - c. Health Actuarial (B) Task Force

Interpretation of the Statutory Accounting Principles Working Group

INT 21-02T: Extension of Ninety-Day Rule for the Impact of Hurricane Ida

INT 21-02T Dates Discussed

Email Vote to Expose Sept. 9, 2021

INT 21-02T References

SSAP No. 6—Uncollected Premium Balances, Bills Receivable for Premiums, and Amounts Due From Agents and Brokers

INT 21-02T Issue

1. Hurricane Ida and its aftermath has resulted in tremendous loss of life and property, the extent to which is currently not known. The Federal Emergency Management Agency (FEMA) lists Louisiana, New Jersey and New York as having emergency declarations because of the hurricane and related flooding. This interpretation is intended to cover storm impacted policies in areas in which a state of emergency was declared. State regulators and insurers are taking action to provide policyholders affected by this disaster with the support and understanding that is deserved.
2. Should a 60-day extension of the 90-day rule for uncollected premiums be temporarily granted to insurers for policies in U.S. jurisdictions where a state of emergency was declared which were affected by the hurricane, its aftermath and related flooding?

INT 21-02T Discussion

3. The Working Group reached a tentative consensus for a one-time optional extension of the ninety-day rule for uncollected premium balances, bills receivable for premiums and amounts due from agents and policyholders required per SSAP No. 6, paragraph 9, as described within this paragraph.
 - a. For policies in effect as of the declaration of a state of emergency by either the states, U.S. territories or federal government, as described in paragraph 1, insurers with policyholders in areas impacted by Hurricane Ida, its aftermath and the related flooding may wait 150 days (90 days per existing guidance, plus a 60-day extension), not to extend beyond Jan. 23, 2022, before nonadmitting premiums receivable from those directly impacted policyholders as required per SSAP No. 6, paragraph 9.
 - b. Existing impairment analysis remains in effect for these affected policies.
4. The Working Group noted that a temporary sixty day (60) extension had previously been provided for other nationally significant disasters including *INT 20-11: Extension of Ninety-Day Rule for the Impact of 2020 Hurricanes, California Wildfires and Iowa Windstorms*, *INT 18-04: Extension of Ninety-Day Rule for the Impact of Hurricane Florence and Hurricane Michael*; *INT 17-01: Extension of Ninety-Day Rule for the Impact of Hurricane Harvey, Hurricane Irma and Hurricane Maria*; *INT 13-01: Extension of Ninety-Day Rule for the Impact of Hurricane/Superstorm Sandy*; and *INT 05-04: Extension of Ninety-day Rule for the Impact of Hurricane Katrina, Hurricane Rita and Hurricane Wilma*.
5. Due to the short-term nature of the applicability of this extension, which expires Jan. 23, 2022, this interpretation will be publicly posted on the Statutory Accounting Principles (E) Working Group web page. This interpretation will be automatically nullified on Jan. 24, 2022, and will be included as a nullified INT in Appendix

INT 21-02T

Interpretations

H – Superseded SSAPs and Nullified Interpretations in the “As of March 2022” *Accounting Practices and Procedures Manual*.

INT 21-02T Status

6. Further discussion is planned.

<https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/NationalMeetings/A.NationalMeetingMaterials/2021/12.NovemberCall/4-INT21-02T-HurricaneIda.docx>

**Statutory Accounting Principles (E) Working Group
November 10, 2021 – Interim Call
Comment Letters Received**

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Interested Parties – October 1, 2021 <ul style="list-style-type: none"> ○ Ref #2021-11: SSAP No. 43R – Credit Tenant Loans - Scope ○ Ref #2021-12EP: Editorial Updates ○ Ref #2021-13: Salvage – Legal Recoveries ○ Ref #2021-14: Policy Statement Terminology Change – Substantive and Nonsubstantive ○ INT 21-02T: INT 21-02T – Hurricane Ida ○ Ref #2019-24: SSAP No. 71 – Levelized and Persistency Commission (Issue Paper) 	5-8

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October 22, 2021

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Ref #2021-15, SSAP No. 43R-Residual Tranches

Dear Mr. Bruggeman:

Interested parties (“IPs”) appreciate the opportunity to comment on the Statutory Accounting Principles Working Group (the Working Group) proposal Ref #2021-15, SSAP No. 43R-Residual Tranches (“the proposal”).

The proposal would require certain modifications to SSAP No. 43R to report non-rated residual tranches or interests, currently in the scope of SSAP No. 43R, on Schedule BA as Other Long-Term Invested Assets at lower of cost or market. Also proposed is that a footnote be added to further define “non-rated residual tranches or interests” as follows:

“Reference to “non-rated residual tranches or interests” intends to capture securitization tranches, beneficial interests, interests of structured finance investments, as well as other structures captured in scope of this statement, that reflect loss layers without contractual interest or principal payments. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.”

IPs have the following comments related to the proposal:

- 1) IPs agree that residual tranches or interests in scope of SSAP No. 43R, which meet the definition in the proposed footnote, should be reported on Schedule BA at lower of cost or market (“LOCOM”).

Some companies already report such investments on Schedule BA and others report them on Schedule D measured at either LOCOM or amortized cost. We believe the proposed

change in reporting would be cost justified as it would not be overly burdensome to insurers and would provide consistent reporting by insurers. It also would provide additional information for regulators to continue to evaluate such investments.

- 2) IPs believe an effective date of 12/31/2021 is achievable with regard to rating all residual tranches in the scope of SSAP No. 43R as NAIC 6. However, for various reasons noted below, IPs do not believe it would be feasible to transfer those residual tranches currently reported on Schedule D to Schedule BA for year-end 2021 reporting.

In conversations with NAIC staff and regulators, while working on the Working Group's Bond Project (formerly known as the 43R Project), IPs have been asked if adopting the proposal effective 12/31/2021 is feasible and also if reporting such interests on Schedule BA separately depending on the underlying collateral (e.g., fixed income, equity, real estate, etc.; same categories that currently exist on Schedule BA) would be feasible beginning at year-end 2022.

IPs believe that the 12/31/2021 reporting is not feasible as it would be operationally difficult to change processes in a timely manner prior to year-end reporting, including any vendor modifications that would be required, as well as address downstream implications such as impacts on cash flow statements and investment schedule rollforwards, etc., to ensure there are no unintended consequences related to the various statutory blanks and related processes. IPs support making such a change beginning at year-end 2022 and support the more granular reporting requested (i.e., based on underlying collateral) as it will allow the requisite amount of time to address those operational items discussed above. IPs also support allowing those companies that can address their processes prior to year-end 2021, the opportunity to transfer the residual tranches in scope from Schedule D to BA in 2021. It is important that the Working Group make companies aware that (1) the transfer of residual tranches to Schedule BA is optional for year-end 2021/quarterly 2022 and (2) if they choose to transfer the residual tranches to Schedule BA at year-end 2021, they would also be required to transfer them at year-end 2022 into the more granular categories discussed above based on underlying collateral (e.g., equities, fixed income, real estate, etc.). For those companies that decide to transfer the residual tranches in 2021, Blanks instructions would be needed well in advance of year-end to provide clarity related to the following:

- The specific section and subsection of Schedule BA where the residual tranches and interests in scope of this proposal would be reported.
- How the various existing columns of Schedule BA would be used for such investments. For example, Schedule BA "cost" would be used to report "amortized cost" for such investments.
- Communicating that LOCOM would be applied to such investments and clarifying where both amortized cost and fair value would be reported on the existing Schedule BA.

- 3) IPs recommend certain modifications to the proposed footnote and changes to SSAP No. 43R as follows:
- Eliminate the reference to “non-rated” in paragraphs 26a, b, and c and the proposed footnote. IPs recommend eliminating the reference to non-rated as its definition may be interpreted inconsistently by various insurers (e.g., rated by the NAIC, rated by an NRSRO, insurer-rated such as NAIC 5 or 6?). We believe the intent is to exclude from Schedule D reporting, those investments that are typically not rated in the investment markets because their characteristics are not debt-like (e.g., no contractual payments of principal and/or interest) and thus we believe the inclusion of only the criteria “no contractual payments of principal and/or interest” will capture all investments intended to be captured.
 - IPs recommend removing the term “structured finance investments” from the footnote as it is an undefined term and is not clear to IPs as to what it is intended to capture. We believe retaining the references to “securitization tranches and beneficial interests” is adequate and would be understood to include all those investments intended by the regulators to be in the scope of the proposal.
 - IPs recommend modifying the footnote to include those investments “...that reflect loss layers without contractual interest or principal payments” to those investments “...that reflect loss layers without any contractual payments, whether principal, interest, or both”. This proposed change would be more complete and “all-encompassing”.
 - Ensure LOCOM is clarified to be “lower of **amortized cost** or market”. The use of the term “amortized cost” versus “cost” more accurately reflects the type of investment and is more aligned with the use of the term in existing SSAP No. 43R.

The following proposal reflects IPs comments discussed above as related to the footnote:

“Reference to “residual tranches or interests” intends to capture securitization tranches and beneficial interests as well as other structures captured in scope of this statement, that reflect loss layers without any contractual payments, whether principal, interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.”

We would be happy to discuss any of our recommendations above and appreciate the continued dialogue related to this topic and the overall Bond Project among the Working Group, NAIC Staff, Regulators, and IPs.

* * *

Statutory Accounting Principles Working Group

October 22, 2021

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Thank you for considering interested parties' comments. If you have any questions in the interim, please do not hesitate to contact us.

Sincerely,

D. Keith Bell

Rose Albrizio

cc: NAIC staff
Interested parties

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October 1, 2021

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Items Exposed for Comment by the Statutory Accounting Principles Working Group on August 26, 2021 with Comments due October 1, 2021

Dear Mr. Bruggeman:

Interested parties appreciate the opportunity to comment on the exposure drafts released for comment by the NAIC Statutory Accounting Principles (E) Working Group (the Working Group). We offer the following comments:

Ref #2021-11 SSAP No. 43R

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed the following:

1. Revisions to *SSAP No. 43R—Loan-Backed and Structured Securities*, as illustrated in the proposal, to explicitly identify the SVO-Identified CTLs that are in scope of SSAP No. 43R. These revisions also propose to delete the examples of “other loan-backed and structured securities” in paragraph 27.b. Comments are requested if this deletion is perceived to remove investments from the scope of SSAP No. 43R.
2. Request for comment on the Working Group’s intent to nullify INT 20-10. (This INT nullifies automatically on Oct. 1, 2021, but it is anticipated that the explicit nullification will identify the revisions adopted by the VOSTF for historical reference.)
3. Disposal of agenda item 2020-24: Accounting and Reporting of Credit Tenant Loans without statutory revisions. This was the agenda item in response to the initial VOSTF referral and is no longer applicable with the adopted Task Force edits to clarify that CTLs are mortgage loans in scope of SSAP No. 37.

Interested parties have no comment on this item.

Ref #2021-12 NAIC Accounting Practices and Procedures Manual Editorial and Maintenance Update

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed editorial revisions to the Preamble, *Appendix A-001: Investments of Reporting Entities*, *Appendix C Actuarial Guidelines – Appendices*, *Appendix C-2 Interpretations of the Emerging Actuarial Issues (E) Working Group*, and *SSAP No. 21R—Other Admitted Assets*, as illustrated in the proposal.

Interested parties have no comment on this item.

Ref #2021-13 SSAP No. 55: Salvage - Legal Recoveries

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and took the following actions:

1. Exposed revisions to *SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*, as illustrated in the proposal, to clarify that salvage and subrogation recoveries should be reported as a reduction of losses and/or loss adjusting expense (LAE reserves), depending on the nature of the costs being recovered. In addition, updates to the disclosure in paragraph 17.h. were exposed.
2. Directed NAIC staff to coordinate develop conforming revisions to the Annual Statement instructions.
3. Directed notification of the exposure to the following actuarial Task Forces:
 - a. Casualty Actuarial and Statistical (C) Task Force,
 - b. Life Actuarial (A) Task Force, and
 - c. Health Actuarial (B) Task Force

Interested parties support this proposal.

Ref #2021-14 Policy Statement Terminology Change – Substantive & Nonsubstantive

The Working Group moved this agenda item to the active listing, categorized as nonsubstantive, and exposed revisions to the *NAIC Policy Statement on Maintenance of Statutory Accounting Principles*, as illustrated in the proposal and suggested by the Financial Condition (E) Committee in their Aug. 14, 2021, referral, to alter the terminology used when discussing types of statutory accounting revisions.

After some discussion and consideration of the proposal and its impact on the implementation of new statutory accounting standards, interested parties concluded that the distinction between substantive (proposed to change to “development of new SSAPs or New SAP Concepts in an

Statutory Accounting Principles Working Group

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Existing SSAPs”) and non-substantive (proposed to change to “Development of SAP Clarifications”) is at times confusing and that there would be more transparency in the development process if the distinction were eliminated. Instead, we recommend that all new standards be handled similarly but that the effective date for each new standard be determined by evaluating the complexity of implementation (e.g., the extent that systems changes are required) and the availability of data to insurers to implement the new standard. This determination would be made as the new standard is being completed and with feedback from industry as to the time needed to adopt the new requirements.

INT 21-02T: Extension of Ninety-Day Rule for the Impact of Hurricane Ida

The Working Group reached a tentative consensus for a one-time optional extension of the ninety-day rule for uncollected premium balances, bills receivable for premiums and amounts due from agents and policyholders required per SSAP No. 6, paragraph 9. For policies in effect as of the declaration of a state of emergency by either the states, U.S. territories or federal government, as described in paragraph 1, insurers with policyholders in areas impacted by Hurricane Ida, its aftermath and the related flooding may wait 150 days (90 days per existing guidance, plus a 60-day extension), not to extend beyond Jan. 23, 2022, before nonadmitting premiums receivable from those directly impacted policyholders as required per SSAP No. 6, paragraph 9. b. Existing impairment analysis remains in effect for these affected policies.

The Working Group noted that a temporary sixty day (60) extension had previously been provided for other nationally significant disasters including INT 20-11: Extension of Ninety-Day Rule for the Impact of 2020 Hurricanes, California Wildfires and Iowa Windstorms, INT 18-04: Extension of Ninety-Day Rule for the Impact of Hurricane Florence and Hurricane Michael; INT 17-01: Extension of Ninety-Day Rule for the Impact of Hurricane Harvey, Hurricane Irma and Hurricane Maria; INT 13-01: Extension of Ninety-Day Rule for the Impact of Hurricane/Superstorm Sandy; and INT 05-04: Extension of Ninety-day Rule for the Impact of Hurricane Katrina, Hurricane Rita and Hurricane Wilma.

This interpretation will be automatically nullified on Jan. 24, 2022 and will be included as a nullified INT in Appendix H – Superseded SSAPs and Nullified Interpretations in the “As of March 2022” *NAIC Accounting Practices and Procedures Manual*.

Interested parties support this proposal.

Ref #2019-24 SSAP No. 71: Levelized Commissions

The Working Group exposed Issue Paper No. 16x: Levelized Commissions to document the historical discussion and final action adopted through the Executive Committee/Plenary.

Interested parties have no further comment on this item.

* * *

Statutory Accounting Principles Working Group

October 1, 2021

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Thank you for considering interested parties' comments. If you have any questions in the interim, please do not hesitate to contact us.

Sincerely,

D. Keith Bell

Rose Albrizio

cc: NAIC staff
Interested parties

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To: Jacob Garn, Chair of the Blanks (E) Working Group
From: Dale Bruggeman, Chair of the Statutory Accounting Principles (E) Working Group
Kevin Fry, Chair of the Valuation of Securities (E) Task Force
Re: Year-End 2021 Reporting for Residual Tranches Retained on Schedule D-1
Date: November 12, 2021

The purpose of this memo is to notify the Blanks (E) Working Group and interested parties on the reporting of residual tranches retained on Schedule D-1: Long-Term Bonds for year-end 2021. Furthermore, it intends to broadly communicate that use of the NAIC 5GI designation process for items that do not have contractual principal or interest payments reflects an incorrect application of the guidance.

As part of the bond proposal project, it was identified that there is inconsistency in practice with how residual tranches or interests are reported within the investment schedules, with some entities reporting on Schedule BA: Other Invested Assets, and other entities reporting on Schedule D-1, with either a self-assigned NAIC 5GI or NAIC 6 designation. Although action taken by the SAPWG will require residual tranches or interests to be reported on Schedule BA for year-end 2022, these items can be retained on Schedule D-1 for year-end 2021. However, if retained on Schedule D-1, the Working Group confirmed with the Securities Valuation Office that use of the NAIC 5GI process for residual tranches is an inaccurate application, and residual tranches or interests reported on Schedule D-1 shall be reported with an NAIC 6 designation. The following information defines residual tranches or interests subject to this clarification as well as why an NAIC 5GI designation cannot be used for these securities:

Residual Tranche / Interests: Reference to “residual tranches or interests” intends to capture securitization tranches and beneficial interests as well as other structures captured in scope of *SSAP No. 43R—Loan-Backed and Structured Securities*, that reflect loss layers without any contractual payments, whether principal or interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

Application of NAIC 5GI: The NAIC 5GI process, noted in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office*, permits entities to self-assign an NAIC 5 when they can certify the following three components: 1) Documentation necessary to permit a full credit analysis of the security does not exist or an NAIC CRP ratings for an FE or PL security is not available. 2) The issuer or obligor is current on all contracted interest and principal payments. 3) The insurer has an actual expectation of ultimate payment of all contracted interest and principal payments. Use of the NAIC 5GI process for residual investments is an incorrect application of the guidance as 1) there are no contracted interest and principal payments to certify as current and 2) the insurer cannot have an actual expectation of receiving all contractual principal and interest of the underlying collateral as these tranches absorb the losses first for the securitization structure. Although cash flows may pass through to these holders at periodic intervals in the waterfall, ultimate returns depend on

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continued performance, therefore, there can be no actual expectation that future payments will be received. The Valuation of Securities (E) Task Force is currently incorporating edits to mitigate future misapplication of the NAIC 5GI process.

Please contact NAIC staff of the SAPWG or VOSTF with any questions.

Cc: Mary Caswell, Calvin Ferguson, Julie Gann, Robin Marcotte, Jim Pinegar, Jake Stultz, Charles Therriault

[https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/Stat_Acctg_Statutory_Referrals/2021/SAPWG to Blanks Nov 2021.docx](https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/Stat_Acctg_Statutory_Referrals/2021/SAPWG%20to%20Blanks%20Nov%202021.docx)

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TO: Kevin Fry, Chair, Valuation of Securities (E) Task Force
FROM: Dale Bruggeman, Chair of the Statutory Accounting Principles (E) Working Group
Carrie Mears, Vice-Chair of the Statutory Accounting Principles (E) Working Group
RE: Provisions for NAIC 5GI Designations
DATE: November 15, 2021

The purpose of this referral is to request that the Valuation of Securities (E) Task Force review the NAIC 5GI guidance detailed in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* and consider whether modifications are necessary to clarify the intent of the guidance and mitigate misapplications. As an example, the Working Group was made aware of situations in which residual tranches, which do not have contractual interest or principal payments, were being designated as NAIC 5GI by reporting entities. Although there was broad agreement by key industry representatives and state insurance regulators that the NAIC 5GI should not be permitted for these residual tranches, potential refinement to clarify the NAIC 5GI provisions may prevent future misapplication.

Residual Tranches Defined per SSAP No. 43R—Loan-Backed and Structured Securities: Reference to “residual tranches or interests” intends to capture securitization tranches and beneficial interests as well as other structures captured in scope of this statement, that reflect loss layers without any contractual payments, whether principal or interest, or both. Payments to holders of these investments occur after contractual interest and principal payments have been made to other tranches or interests and are based on the remaining available funds. Although payments to holders can occur throughout an investment’s duration (and not just at maturity), such instances still reflect the residual amount permitted to be distributed after other holders have received contractual interest and principal payments.

In addition to clarifying that the guidance cannot be applied to residual tranches, as defined in SSAP No. 43R, the following concepts are provided as suggestions for possible clarification:

- Clarifications to ensure that the NAIC 5GI self-assigned designation is permitted only for securities that could be reviewed for an NAIC designation if the documentation to support a credit analysis could be submitted. In other words, the 5GI process is not intended to be used for securities that would not qualify for a designation even if a full credit analysis could be performed. Securities that cannot be reviewed for an NAIC designation due to the lack of a process / methodology for the type of security or structure are not permitted to be self-assigned an NAIC 5GI designation.
- Clarification that self-assigning an NAIC 6* for securities that do not qualify for NAIC 5GI is not a declaration of potential default. Rather, the self-assignment indicates that the security

could not be reviewed for a full credit analysis and the requirements for an NAIC 5GI could not be met.

Thank you for considering these potential clarifications. Please contact Dale Bruggeman, or Carrie Mears, SAPWG Chair and Vice Chair, with any questions.

Cc: Julie Gann, Robin Marcotte, Jim Pinegar, Jake Stultz, Charles Therriault, Marc Pearlman

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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, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

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

RE: Non-substantive technical amendment to the P&P Manual for Private Letter Rating Securities and the corresponding NAIC Designation Category for NAIC 5GI

DATE: November 1, 2021

Summary – At the May 24, 2021 Task Force meeting the Task Force adopted an amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) requiring the submission of Private Rating Letter Rationale Reports with certain Private Rating Letters filed with the SVO. In the May amendment certain language, currently in the printed December 2020 version of the P&P, which clarifies that an NAIC 5GI Designation is the equivalent of an NAIC 5.B Designation Category, was erroneously omitted. The SVO proposes a non-substantive technical amendment to the May amendment by re-inserting the omitted language as shown below in **red** (additions **underlined** and deletions with **strikethrough**), as well as including identical language in one paragraph adopted pursuant to the May 2021 amendment.

PART THREE
SVO PROCEDURES AND METHODOLOGY FOR PRODUCTION
OF NAIC DESIGNATIONS

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

...

PL SECURITIES

...

12. For (a) PL Securities issued from January 1, 2018 to December 31, 2021 subject to a confidentiality agreement executed prior to January 1, 2022, which confidentiality agreement remains in force, for which an insurance company cannot provide a copy of a private rating letter rationale report to the SVO due to confidentiality or other contractual reasons (“waived submission PLR securities”), the insurer may report such securities on such securities’ General Interrogatory (i.e., a **PLGI** security), and (b) PL Securities issued after January 1, 2022, for which an insurance company cannot provide a copy of a private rating letter rationale report to the SVO due to confidentiality or other contractual reasons (“deferred submission PLR securities”) the insurer may report such securities on such securities’ General Interrogatory (i.e., a **PLGI** security) until and including December 31, 2023, after which time, if the insurance company still cannot provide a copy of a private rating letter rationale report for whatever reason, the securities can be reported with an NAIC 5GI Designation and an NAIC Designation Category of NAIC 5.B GI in accordance with the guidance specified below.

...

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

...

16. 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** and an NAIC Designation Category of NAIC 5.B GI to the security and report using the Interrogatory procedure; in either case within 120 days of purchase.

Producing NAIC Designations for PL Securities

...

22. 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
- 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 and an NAIC Designation Category of NAIC 5.B GI to the security in the related Interrogatory.

If the SVO deems a security ineligible to receive an NAIC Designation per the instructions in this Manual because (a) the security is ineligible for Filing Exception according to “Specific Populations of Securities Not Eligible for Filing Exemption” in this Part or (b) the security is of a type outside the scope of *SSAP No. 26R - Bonds, SSAP No. 32- Preferred Stock, or SSAP No. 43R – Loan Backed and Structured Securities* then, for such a security, the SVO will provide a brief explanation in VISION, accessible to all VISION account holders, of why the security will not be provided an NAIC Designation.

23. An **NAIC 5GI** Designation and an NAIC Designation Category of NAIC 5.B GI 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 (a) 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, (b) for private letter ratings issued on or after January 1, 2022, an insurance company does not provide a copy of a private rating letter rationale report to the SVO for which there are no confidentiality or contractual limitations or (c) for deferred submission PLR securities, if the insurance company does not submit the private rating letter rationale report to the SVO on or after January 1, 2024.