NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Date: 6/4/2024

Valuation of Securities (E) Task Force
Tuesday, June 18, 2024
3:00 p.m. - 4:00 p.m. ET / 2:00 p.m. - 3:00 p.m. CT / 1:00 p.m. - 2:00 p.m. MT / 12:00 p.m. - 1:00 p.m. PT

ROLL CALL

Member	**Representative**	**State**
Doug Ommen, Chair	Carrie Mears	Iowa
Eric Dunning, Vice Chair	Lindsay Crawford	Nebraska
Mark Fowler	Sheila Travis	Alabama
Lori K. Wing-Heier	David Phifer	Alaska
Ricardo Lara	Laura Clements	California
Andrew N. Mais	Ken Cotrone	Connecticut
Michael Yaworsky	Ray Spudeck	Florida
Dean L. Cameron	Eric Fletcher	Idaho
Ann Gillespie, Acting Director	Vincent Tsang	Illinois
Vicki Schmidt	Tish Becker	Kansas
Timothy J. Temple	Stewart Guerin	Louisiana
Kathleen A. Birrane	Gregory Ricci	Maryland
Rachel Davison, Acting Commissioner	John Turchi	Massachusetts
Grace Arnold	Fred Andersen	Minnesota
Chlora Lindley-Myers	Debbie Doggett	Missouri
D.J. Bettencourt	Jennifer Li	New Hampshire
Justin Zimmerman	John Sirovetz	New Jersey
Adrienne A. Harris	Robert Kasinow James Everett	New York
Jon Godfread	Matt Fischer	North Dakota
Judith L. French	Tom Botsko	Ohio
Glen Mulready	Diane Carter	Oklahoma
Michael Humphreys	Diana Sherman	Pennsylvania
Cassie Brown	Amy Garcia	Texas
Jon Pike	Jake Garn	Utah
Scott A. White	Doug Stolte	Virginia
Mike Kreidler	Katy Bardsley	Washington
Nathan Houdek	Amy Malm	Wisconsin

NAIC Support Staff: Charles Therriault/Marc Perlman

AGENDA

Discuss and Consider for Adoption:

1. Proposed P&P Manual Amendment to Permit NAIC Designations for Short-term ABS (Doc. ID: 2024-005.01, 2024-005.02) —Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment A, A-1

2. Proposed P&P Manual Amendment to Add Spain to the List of Foreign (Non-U.S.) Jurisdictions Eligible for Netting for Purposes of Determining Exposures to Counterparties for Schedule DB, Part D, Section 1
(Doc. ID: 2024-006.01, 2024-006.02)
—Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment B, B-1

3. Proposed P&P Manual Amendment to Change the Effective Date for the Implementation of CLO Modeling
(Doc. ID: 2024-007.01, 2024-007.02)
—Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment C, C-1

4. Proposed P&P Manual Amendment to Clarify Permitting Insurers to Self-assign an NAIC Designation 6*
(Doc. ID: 2024-008.01, 2024-008.02)
—Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment D, D-1

5. Proposed P&P Manual Amendment to Make Current the List of SVO Processes
(Doc. ID: 2024-009.01, 2024-009.02)
—Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment E, E-1

Receive and Consider for Exposure:

6. Revised Proposed P&P Manual Amendment to Update the Definition of an NAIC Designation
(Doc. ID: 2022-012.12)
—Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment F

7. Revised Proposed P&P Manual Amendment Authorizing the Procedures for the SVO's Discretion Over NAIC Designations Assigned Through the Filing Exemption Process
(Doc. ID: 2023-005.16)
—Carrie Mears (IA), Charles A. Therriault (NAIC), and Marc Perlman (NAIC) — Attachment G

Hear Staff Report:

8. Updates on the Proposed CLO Modeling Methodology and Ad-hoc Working Group
—Eric Kolchinsky (NAIC)

9. Any other matters

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, 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: Proposed P&P Manual Amendment to Permit NAIC Designations for Short-term ABS

DATE: April 16, 2024

Summary: The Statutory Accounting Principles (E) Working Group adopted revisions to SSAP No. 2R - *Cash, Cash Equivalents, Drafts and Short Term Investments* in the Accounting Practices & Procedures Manual (AP&P) on Dec. 1, 2023. The revisions, which will be effective Jan. 1, 2025, further restrict the investments that are permitted for cash equivalent or short-term investment reporting. The revisions are below in their final form with highlights in **bold underline** added.

Adopted revisions to SSAP No. 2R:

…

Cash Equivalents

6. Cash equivalents are short-term, highly liquid investments that are both (a) readily convertible to known amounts of cash, and (b) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Only investments with original maturities of three months or less can qualify under this definition, with the exception of money market mutual funds, as detailed in paragraph 8, and cash pooling, as detailed in paragraph 9. Certificates of deposit with a maturity of less than 12 months at the time of acquisition are reported as cash pursuant to paragraph 5. **Regardless of maturity date, the following investments are not permitted to be reported as cash equivalents** and shall be reported on the investment schedule that corresponds to the SSAP for which the investment is applicable:

a. Asset-backed securities captured in scope of SSAP No. 43R.

b. All investments that are reported on Schedule BA, including but not limited to:

i. All debt securities that do not qualify as bonds in scope of SSAP No. 21R.

ii. Collateral/Non-Collateral loans captured in scope of SSAP No. 21R.

iii. Working capital finance investments in scope of SSAP No. 105R.

iv. Surplus notes in scope of SSAP No. 41

c. Mortgage loans captured in scope of SSAP No. 37.

d. Derivative instruments in scope of SSAP No. 86 or SSAP No. 108.

e. Securities with terms that are reset at predefined dates (e.g., an auction-rate security that has a long-term maturity and an interest rate that is regularly reset through a Dutch auction) or have other features an investor may believe results in a different term than the related contractual maturity shall be accounted for based on the contractual maturity at the date of acquisition, except where other specific rules within the statutory accounting framework currently exist.

…

Short-Term Investments

14. Short-term investments are investments that do not qualify as cash equivalents, but that are still considered highly liquid as they have remaining maturities (or repurchase dates under reverse repurchase agreements) of one year or less at the time of acquisition. Certificates of deposit with a maturity of less than 12 months at the time of acquisition are reported as cash pursuant to paragraph 5. **Regardless of maturity date, the following investments are not permitted to be reported as short-term investments** and shall be reported on the investment schedule that corresponds to the SSAP for which the investment is applicable:

a. Asset-backed securities captured in scope of SSAP No. 43R.

b. All investments that are reported on Schedule BA, including but not limited to:

i. All debt securities that do not qualify as bonds in scope of SSAP No. 21R.

ii. Collateral/Non-Collateral loans captured in scope of SSAP No. 20R or 21R.

iii. Working capital finance investments in scope of SSAP No. 105R.

iv. Surplus notes in scope of SSAP No. 41R.

c. Mortgage loans captured in scope of SSAP No. 37.

d. Derivative instruments in scope of SSAP No. 86 or SSAP No. 108.

…

Asset-backed securities captured within scope of what will be the revised SSAP No. 43 – *Asset Backed Securities,* as of Jan. 1, 2025, are expressly excluded from the definition of Cash Equivalents and Short-Term Investments. This amendment proposes to permit the assignment of an NAIC Designation to these investments if they are captured within the scope of the revised SSAP No. 43 – *Asset Backed Securities* and are eligible to be reported on Schedule D, Part 1, Sub-part 2 as an Asset Backed Security.

Recommendation: The Securities Valuation Office (SVO) recommends adoption of this conforming amendment to permit securities that qualify under SSAP No. 43 – *Asset Backed Securities* to be reported with an NAIC Designation and NAIC Designation Category assigned in compliance with the guidance in the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual). The proposed text changes to the P&P Manual are shown below with additions in red underline and deletions in ~~red strikethrough~~, as it would appear in the 2023 P&P Manual.

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

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

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

SPECIAL INSTRUCTIONS

Short-Term Investments

128. A short-term investment is defined as an investment that has one year or less to maturity. Investments that have one year or less to maturity when issued are not reported to the SVO. Investments, which when acquired by an insurance company have one year or less to maturity, but which when issued had greater than one year to maturity, need only be reported to the SVO if they do not have an NAIC CRP rating or an NAIC Designation for the issuer. This guidance excludes investments that are captured in scope of *SSAP No. 43 – Asset Backed Securities.* Investments that are captured in scope of *SSAP No. 43 – Asset Backed Securities* shall follow the guidance in this Manual for the assignment of an NAIC Designation and NAIC Designation Category.

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2024/2024-05-02 VOSTF Interim Meeting/03-Short-term ABS/2024-005.01 PP Manual Short-term ABS v2.docx

ACLI Financial Security for Life | PPiA Private Placement investors Association | NASVA

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

June 2, 2024

Ms. Carrie Mears
Chair, Valuation of Securities (E) Task Force (VOSTF)
National Association of Insurance Commissioners (NAIC)
110 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Proposed P&P Manual Amendment to Permit NAIC Designations for Short-term ABS

Dear Ms. Mears:

The undersigned (ACLI, PPIA, and NASVA) appreciate the opportunity to comment on the exposure referred to above that was released for comment by the VOSTF on May 2, 2024.

We support the exposure as drafted. ACLI is very appreciative and supportive of the VOSTF. ACLI stands ready to continue working with the NAIC.

If you have any questions regarding this letter, please do not hesitate to contact us.

Sincerely,

Mike Monahan
ACLI

Tracey Lindsey
Tracey Lindsey
NASVA

John Petchler
John Petchler
on behalf of PPiA Board of Directors

cc: Charles Therriault, Director, Securities Valuation Office
Eric Kolchinsky, Director, Structured Securities Group

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, 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: Proposed amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the "P&P Manual") to add Spain to the list of jurisdictions eligible for counterparty exposure netting

DATE: April 8, 2024

Summary –

Banco Bilbao Vizcaya Argentaria, S.A. ("BBVA"), a bank organized under the laws of the Kingdom of Spain, has requested the addition of Spain to the P&P Manual's list of jurisdictions eligible for counterparty close-out netting.

The purpose of identifying jurisdictions eligible for close-out netting is to permit the calculation of credit risk exposures to counterparties in Schedule DB, Part D, Section 1. The netting of offsetting liabilities with a counterparty will only be permitted in that Schedule if there exists a master agreement that provides for such netting and if there is adequate legal certainty that closeout netting would be enforced upon default of the counterparty. The P&P Manual provides for the addition of jurisdictions to the list of jurisdictions eligible for close-out netting if, in the SVO's opinion, legal opinions and/or other analysis provides adequate legal certainty that, upon default of the counterparty, closeout netting would be enforced.

In support of its application, BBVA submitted a legal opinion of the law firm Clifford Chance, S.L.P. on the validity and enforceability of close-out netting provisions under Spanish law. The opinion was commissioned by the International Swaps and Derivatives Association (ISDA), a private trade organization whose mission is to foster safe and efficient derivatives markets, in part through the development of standardized documentation. ISDA netting opinions are widely and accepted by regulators around the globe, specifically by banking regulators.

Each of the netting opinions commissioned by ISDA, including the Spanish opinion, spell out various parameters, specific to the laws of the relevant jurisdiction, which a master agreement must meet to be consistent with the opinion. For example, according to the Spanish opinion, there are different requirements for netting enforceability depending on whether the insolvent Spanish counterparty is or is not a Spanish bank, credit institution, investment firm or broker dealer. It would be impracticable to expect the SVO to review all master agreements for compliance with the parameters delineated in the netting opinion for the relevant jurisdiction. Therefore, we propose amending the netting eligibility section of the P&P Manual to include a proviso that it is assumed that each master agreement complies with the parameters delineated in the netting opinion for the relevant jurisdiction.

Upon its review of the Spanish law opinion, the SVO has determined that it provides adequate legal certainty that closeout netting would be enforced (assuming, that master agreement provisions are consistent with the parameters explained in the netting opinion) and proposes adding Spain to the list of jurisdictions eligible for counterparty exposure netting.

Proposed Amendment - The proposed text changes to the P&P Manual are shown below with additions in red font color and deletions in ~~red strikethrough~~, as it would appear in the 2023 P&P Manual format.

PART TWO
OPERATIONAL AND ADMINISTRATIVE INSTRUCTION
APPLICABLE TO THE SVO

COUNTERPARTY EXPOSURE; NETTING ELIGIBILITY

. . .

Netting Eligibility

. . .

139. The VOS/TF has determined that there is adequate legal certainty to permit netting of exposures for counterparties domiciled within the United States. Netting of exposures for a foreign (non-U.S.) counterparty will be permitted if its domiciliary jurisdiction has been approved for listing in the List of Jurisdictions Eligible for Netting. Other jurisdictions may be added to the List of Jurisdictions Eligible for Netting if, in the opinion of the SVO, after consultation with the VOS/TF, legal opinions or analyses provide adequate legal certainty that upon default of the counterparty, close-out netting would be enforceable. The SVO's opinion of adequate legal certainty is based on the assumption, authorized by the VOS/TF, that each master agreement will comply with any parameters delineated in the netting opinion for its relevant jurisdiction.

. . .

LIST OF FOREIGN (NON-U.S.) JURISDICTIONS ELIGIBLE FOR NETTING FOR PURPOSES OF DETERMINING EXPOSURES TO COUNTERPARTIES FOR SCHEDULE DB, PART D, SECTION 1

Procedures for Determining NAIC Designations and Netting Eligibility for Derivate Instrument Counterparties

146. **Netting Eligibility** – The purpose of identifying jurisdictions eligible for netting is to permit the calculation of credit risk exposures to counterparties in Schedule DB, Part D, Section 1. The netting of offsetting liabilities with a counterparty will only be permitted in this Schedule if there exists a master agreement that provides for such netting and if there is adequate legal certainty that closeout netting would be enforced upon default of the counterparty.

147. **Legal Certainty for Netting Eligibility –** There is adequate legal certainty to permit netting of exposures for counterparties domiciled within the United States. Netting of exposures in Schedule DB, Part D, Section 1 will be permitted for a foreign (non-U.S.) counterparty if its domiciliary jurisdiction appears on the list in this subparagraph. Jurisdictions will appear on the list if, in the opinion of the SVO, legal opinions and/or analyses provide adequate legal certainty that upon default of the counterparty, closeout netting would be enforced. The SVO's opinion of adequate legal certainty is based on the assumption, authorized by the VOS/TF, that each master agreement will comply with any parameters delineated in the netting opinion for its relevant jurisdiction.

Jurisdiction
Australia
Belgium
Canada
Cayman Island
England
France
Germany
Ireland
Japan
Scotland
Singapore
Spain
Switzerland

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2024/2024-05-02 VOSTF Interim Meeting/04-Spain Netting/2024-004.08 P&P_Spain_Netting.docx

ACLI Financial Security for Life | PPiA Private Placement investors Association | NASVA

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

June 2, 2024

Ms. Carrie Mears
Chair, Valuation of Securities (E) Task Force (VOSTF)
National Association of Insurance Commissioners (NAIC)
110 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Proposed amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the "P&P Manual") to add Spain to the list of jurisdictions eligible for counterparty exposure netting

Dear Ms. Mears:

The undersigned (ACLI, PPIA, and NASVA) appreciate the opportunity to comment on the exposure referred to above that was released for comment by the VOSTF on May 2, 2024.

We support the exposure as drafted. ACLI is very appreciative and supportive of the VOSTF. ACLI stands ready to continue working with the NAIC.

If you have any questions regarding this letter, please do not hesitate to contact us.

Sincerely,

M Monahan

Mike Monahan
ACLI

Tracey Lindsey

Tracey Lindsey
NASVA

John Petchler

John Petchler
on behalf of PPiA Board of Directors

cc: Charles Therriault, Director, Securities Valuation Office
Eric Kolchinsky, Director, Structured Securities Group

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, 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: P&P Manual Amendment to Change the Effective Date for the Financial Modeling of CLOs by SSG to 2025

DATE: April 16, 2024

Summary: At the 2024 Spring National Meeting the Structured Securities Group (SSG) requested a change to the effective date for the financial modeling of collateralized loan obligations (CLOs) to assign NAIC Designations and NAIC Designation Categories to year-end 2025 from year-end 2024. The Task Force agreed to this change. The additional time will permit SSG to improve the methodology and allow better alignment with the approach of other NAIC workstreams.

Recommendation: The Securities Valuation Office (SVO) recommends inclusion of the attached notice in the 2024 *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) informing insurers of the implementation date change and including it on the Task Force's webpage of Adopted Interim Changes to the P&P Manual. The proposed text changes to the P&P Manual are shown below with additions in red underline and deletions in ~~red strikethrough~~, as it would appear in the 2023 P&P Manual.

PREVIOUSLY ADOPTED AMENDMENTS TO THE P&P MANUAL EFFECTIVE IN ~~2024~~ 2025

The following amendments were adopted by the VOS/TF in 2023 to be effective for ~~2024~~ 2025.

- **Adopted an amendment including Collateralized Loan Obligations (CLO) as a Financially Model Security in Part Four** – A collateralized loan obligation (CLO) is type of structured security backed by a pool of debt, typically corporate loans with low credit ratings. An insurer that purchases every tranche of a CLO holds the exact same investment risk as if it had directly purchased the entire pool of loans backing the CLO. The aggregate risk-based capital (RBC) factor for owning all of the CLO tranches should be the same as that required for owning all of the underlying loan collateral. If it is less, it means there is risk-based capital (RBC) arbitrage. As noted in the Investment Analysis Office's (IAO) memo of May 25, 2022, "Risk Assessment of Structured Securities – CLOs", it is currently possible to materially (and artificially) reduce C1 capital requirements just by securitizing a pool of assets. The Task Force assigned the Structured Securities Group (SSG) the responsibility of financially modeling CLO investments and evaluating all tranche level losses across all debt and equity tranches under a series of calibrated and weighted collateral stress scenarios to assign NAIC Designations that create equivalency between securitization and direct holdings, thereby eliminating RBC arbitrage. This amendment is effective beginning with year-end ~~2024~~2025.

The Valuation of Securities (E) Task Force adopted this amendment on Feb. 21, 2023

PART FOUR
THE NAIC STRUCTURED SECURITIES GROUP

. . .

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

. . .

24. Beginning with year-end ~~2024~~ 2025 for CLOs, probability weighted net present values will be produced under NAIC staff supervision by SSG using its financial model with defined analytical inputs selected by the SSG. SSG will model CLO investments and evaluate all tranche level losses across all debt and equity tranches under a series of calibrated and weighted collateral stress scenarios to assign NAIC Designation Categories for a specific CLO tranche as determined by the NAIC.

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

    NOTE: Effective as of January 1, ~~2024~~ 2025, SSG will financially model CLOs.

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2024/2024-05-02 VOSTF Interim Meeting/05-CLO Effective Date/2024-007.01 PP Manual CLO Effective Date.docx

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

June 2, 2024

Ms. Carrie Mears
Chair, Valuation of Securities (E) Task Force (VOSTF)
National Association of Insurance Commissioners (NAIC)
110 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: P&P Manual Amendment to Change the Effective Date for the Financial Modeling of CLOs by SSG to 2025

Dear Ms. Mears:

The undersigned (ACLI, PPIA, and NASVA) appreciate the opportunity to comment on the exposure referred to above that was released for comment by the VOSTF on May 2, 2024.

We support the exposure as drafted. ACLI is very appreciative and supportive of the VOSTF. ACLI stands ready to continue working with the NAIC.

If you have any questions regarding this letter, please do not hesitate to contact us.

Sincerely,

Tracey Lindsey | John Petchler

Mike Monahan
ACLI

Tracey Lindsey
NASVA

John Petchler
on behalf of PPiA Board of Directors

cc: Charles Therriault, Director, Securities Valuation Office
Eric Kolchinsky, Director, Structured Securities Group

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, 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: Proposed P&P Manual Amendment to Clarify that an NAIC Designation 6* can be Self-assigned

DATE: April 16, 2024

Summary: The Securities Valuation Office (SVO) was requested to review the instructions for the self-assignment by insurers of the NAIC 6* Designation. An NAIC 6* can be self-assigned. An NAIC 6* can be self-assigned by an insurer 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 5.B GI are not met. An NAIC 6* can also be self-assigned when the security is deemed to possess the credit characteristics of securities assigned an NAIC 6, meaning the obligation is in or near default and payment of interest, principal or both is not being made, or will not be made, in accordance with the contractual agreement. An NAIC 6 obligation should incur the most severe treatment under the NAIC Financial Regulation Standards and Accreditation Program.

Recommendation: The SVO recommends the attached non-substantive updates to improve the clarity of the instructions for the self-assignment of an NAIC Designation of 6*. The proposed text changes to the P&P Manual are shown below with additions in red underline and deletions in ~~red strikethrough~~, as it would appear in the 2023 P&P Manual format. Editing notes have been added with [ ] to explain section moves. New text is highlighted in yellow.

PART TWO
OPERATIONAL AND ADMINISTRATIVE INSTRUCTIONS APPLICABLE TO THE SVO

PRODUCTION OF NAIC DESIGNATIONS

…

NAIC DESIGNATIONS RELATED TO SPECIAL REPORTING INSTRUCTION

…

~~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 5.B GI are not met.~~ [*Moving the paragraph to keep the NAIC 6* instructions together.*]

…

30. NAIC 6* is self-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 5.B GI are not met.

31. Securities with self-assigned 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.

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2024/2024-05-02 VOSTF Interim Meeting/06-NAIC 6/2024-008-01 P&P Manual - NAIC 6.docx

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

June 2, 2024

Ms. Carrie Mears
Chair, Valuation of Securities (E) Task Force (VOSTF)
National Association of Insurance Commissioners (NAIC)
110 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Proposed P&P Manual Amendment to Clarify that an NAIC Designation 6* can be Self-assigned

Dear Ms. Mears:

The undersigned (ACLI, PPIA, and NASVA) appreciate the opportunity to comment on the exposure referred to above that was released for comment by the VOSTF on May 2, 2024.

We support the exposure as drafted. ACLI is very appreciative and supportive of the VOSTF. ACLI stands ready to continue working with the NAIC.

If you have any questions regarding this letter, please do not hesitate to contact us.

Sincerely,

MMonahan
Mike Monahan
ACLI

Tracey Lindsey
Tracey Lindsey
NASVA

John Petchler
John Petchler
on behalf of PPiA Board of Directors

cc: Charles Therriault, Director, Securities Valuation Office
Eric Kolchinsky, Director, Structured Securities Group

SVO

NAIC
NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

TO: Carrie Mears, 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: P&P Manual Amendment to Make Current the List of SVO Processes

DATE: April 16, 2024

Summary and Recommendation: The *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) references several processes by which the SVO identifies information, entities or securities for various lists for publication as part of its Compilation and Publication of the SVO List of Investment Securities responsibilities. We propose updating this section of the P&P Manual to remove those processes which the SVO no longer undertakes and to insert those processes which the SVO does perform but which are missing. Additionally, we propose revising the name of a list related to one of the SVO processes, the “List of Counterparties Rated by the SVO,” to the “List of Counterparties Designated by the SVO,” since the SVO produces Designations which are distinct from rating agency ratings.

The proposed text changes to the P&P Manual are shown below with additions in red underline and deletions in ~~red strikethrough~~, as it would appear in the 2023 P&P Manual.

PART TWO
OPERATIONAL AND ADMINISTRATIVE INSTRUCTIONS APPLICABLE TO THE SVO

COMPILATION AND PUBLICATION OF THE SVO LIST OF INVESTMENT SECURITIES

Directive

3. On a quarterly basis, the SVO shall:

- Compile a list of Investment Securities from each of the data files defined as VOS Process, Filing Exempt Securities Process, CLO/RMBS/CMBS Modeled Securities Process, U.S. Treasury Process and the Exempt U.S. Government Securities Process (each an SVO Sub-List bearing the name of the corresponding Process).

- Exercise best efforts to identify any security in the VOS Process that has been filed by an insurance company without a valuation and to attempt to assign that security a valuation. The SVO may use whatever methodology may seem reasonable to it and may choose not to assign a valuation if doing so would be unreasonable. The VOS/TF considers that an imprecise valuation is of greater utility to the regulatory community than no valuation. However, the NAIC makes no representation that the SVO has the necessary expertise to produce accurate valuations. Accordingly, an insurance company that owns a security to which the SVO has assigned a value under this provision may substitute the SVO assigned value by obtaining or deriving a valuation in accordance with applicable NAIC annual statement reporting instructions and by reporting the valuation obtained to its insurance department on the NAIC Statement Blank.

- Aggregate the content of each SVO Sub-List into a single SVO List of Investment Securities (hereafter, the SVO List of Investment Securities) identifying each Investment Security by name and other pertinent information and showing the NAIC Designation assigned to them by the SVO or pursuant to such other methodology or procedure specified in this Manual.

- Compile, or cause to be compiled, sub-lists from the informational content of the ~~Derivative~~ Counterparties Designated by the SVO ~~P~~process~~, Exchange Rates Process, Ex-Dividend Process,~~ ~~Letter of Credit~~ the Qualified U.S. Financial Institutions ~~P~~process, ~~Money Market and Exchange Traded~~ the Funds ~~P~~process, the Credit Ratings Eligible for Translation to NAIC Designations process, the Sovereign NAIC Designation Equivalent process, and the RSAT Index process ~~and Surplus Notes Processes~~, and any other SVO processes mandated by this Manual (each an SVO Sub-List bearing the name of the corresponding Process and collectively the "Other Information").

- Publish, or cause the SVO List of Investment Securities and the Other Information to be published, by being incorporated into the NAIC's AVS+ product.

. . .

Administration

143. **Listing a Counterparty** – An insurance company that wants to have a counterparty listed on the List of Counterparties ~~Rated~~ Designated by the SVO for Schedule DB, Part D, Section 1 shall submit to the SVO:

- A Counterparty Rating ATF Initial Filing Form.
- Form CRR 1.
- Evidence of an NAIC CRP counterparty rating, an NAIC CRP senior unsecured rating or a copy of the most recent Audited Financial Statement for the counterparty, or the counterparty's guarantor, so that the SVO can assess credit quality and assign an NAIC Designation.
- Upon receipt of the above documents, the SVO shall convert the NAIC CRP rating into its equivalent NAIC Designation or perform a financial analysis of the counterparty, or the counterparty's guarantor, in order to assign an NAIC Designation.

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2024/2024-05-02 VOSTF Interim Meeting/07-SVO Lists/2024-009.01 PP Manual SVOProcessesAmendmentv2.docx

ACLI Financial Security for Life | PPiA Private Placement investors Association | NASVA

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

June 2, 2024

Ms. Carrie Mears
Chair, Valuation of Securities (E) Task Force (VOSTF)
National Association of Insurance Commissioners (NAIC)
110 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: P&P Manual Amendment to Make Current the List of SVO Processes

Dear Ms. Mears:

The undersigned (ACLI, PPIA, and NASVA) appreciate the opportunity to comment on the exposure referred to above that was released for comment by the VOSTF on May 2, 2024.

We support the exposure as drafted. ACLI is very appreciative and supportive of the VOSTF. ACLI stands ready to continue working with the NAIC.

If you have any questions regarding this letter, please do not hesitate to contact us.

Sincerely,

MMonahan
Mike Monahan
ACLI

Tracey Lindsey
Tracey Lindsey
NASVA

John Petchler
John Petchler
on behalf of PPiA Board of Directors

cc: Charles Therriault, Director, Securities Valuation Office
Eric Kolchinsky, Director, Structured Securities Group

SVO

NAIC
NATIONAL ASSOCIATION OF
INSURANCE COMMISSIONERS

TO: Carrie Mears, 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: Proposed Amendment to Update the Definition of an NAIC Designation in the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual)

DATE: June 4, 2023

Summary –

NAIC Designations are currently explained and defined in both Parts One and Two of the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual). The SVO proposes both consolidating these explanations and definitions in Part One only and clarifying the meaning of an NAIC Designation including their use, purpose and risks addressed.

When the new format for the P&P Manual was adopted on November 16, 2018, and published in the new format on April 7, 2019, several changes were made in an attempt to simplify the P&P Manual. It has since become apparent that some of those changes have led to the interpretation that there are two meanings of an NAIC Designation: one meaning, found in Part One, applicable to all securities, whether assigned NAIC Designations pursuant to the Filing Exemption process or by the Securities Valuation Office ("SVO") and a second meaning, found in Part Two, applicable only to securities assigned NAIC Designations by the SVO. It is the SVO staff's belief that there is only one definition of an NAIC Designation and that it is applicable however the NAIC Designation is assigned. To that end, the revisions proposed in this amendment have consolidated the instructions that define an NAIC Designation to make a single uniform definition and includes updates to the definition to address questions and concerns raised about the purpose of NAIC Designations versus credit rating provider ratings.

At the Summer National Meeting held on Aug. 14, 2023, the Task Force discussed an initial draft of a proposed amendment to the P&P Manual updating the definition of an NAIC Designation. The Task Force directed the SVO staff to consider the feedback from Task Force members and interested parties and update the proposal. During and following the March 16, 2024 Spring National Meeting the Task Force received additional comments on the updated amendment. The revised amendment in this memorandum reflects the actionable comments received from Task Force members and interested parties during each comment period including:

1. Creation of a concise definition of an NAIC Designation which focuses on the likelihood that an insurer will receive full and timely principal and expected interest. This change reflects a departure from the term "credit risk" which focuses on the ability of an issuer to make payments in accordance with contractual terms. Credit risk alone may, at times, be too narrow a concept for NAIC purposes. For example, the performance component of a principal protected security (PPS) may produce no return and, therefore, the PPS could pay no interest with no event of default by the issuer. As such, focusing solely on credit risk could limit the SVO's ability to assess the risk of the performance component of a principal protected security.

2. Revisions to the regulatory objective to clarify that an objective of the Task Force is to support regulators in the assessment of the financial ability of an insurer to maintain financial solvency.

3. Removal of the current regulatory assumption that debt instruments pay scheduled interest and principal at maturity.

4. Removal of the application of Subscript S for other non-payment risks and the concept of "other non-payment risks". If this amendment is adopted, any remaining P&P Manual references to Subscript S would be removed in a subsequent amendment.

Proposed Amendment - The proposed text changes to the P&P Manual are shown below with additions in red font color, new text from the last presented iteration of the proposal and deletions in red underline and text deleted from the last presented iteration of the proposal in ~~red strikethrough~~, as it would appear in the 2023 P&P Manual format. Editing notes have been added with *[ ]* to explain section moves.

(VERSION WITH CHANGES DISPLAYED)

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

POLICIES PERTAINING TO SVO AND SSG OPERATIONS

. . .

~~NAIC Designations~~

[Editing note: select portions moved from Part One, paras. 37-39 to the new "NAIC Designations" section within Part One]

37. ~~The SVO's analysis of credit risk (hereafter defined), is expressed as an opinion of credit quality by assignment of an NAIC Designation that is notched to reflect the position of the specific liability in the issuer's capital structure. Collectively, NAIC Designations as defined in this Manual describe a credit quality-risk gradation range from highest quality (least risk) to lowest quality (greatest risk). NAIC Designations express opinions about credit risk except when accompanied by the NAIC Designation subscript, described below.~~

    - ~~Credit risk is defined as the relative financial capability of an obligor to make the payments contractually promised to a lender. Credit analysis is performed solely for the purpose of designating the quality of an investment made by an insurance company so that the NAIC member's department of insurance can better identify regulatory treatment.~~
    - ~~Credit risk is assessed by analyzing the information and documentation provided to the SVO by the reporting insurance company and its advisors. The SVO does not audit the information submitted and assumes the information to be timely, accurate and reliable.~~
    - ~~The ability of an insurance company to realize payment on a financial obligation can be affected by factors not related to credit risk or by the manner in which the repayment promise has been structured.~~
    - ~~NAIC Designations do not measure other risks or factors that may affect repayment, such as volatility/interest rate, prepayment, extension or liquidity risk.~~
    - ~~An NAIC Designation must be interpreted by the NAIC member in context of the NAIC Financial Regulation Standards and Accreditation Program, other characteristics of the investment, and the specific financial and regulatory status of the insurance company.~~

38. ~~The result of the SVO's credit analysis, expressed as an opinion of credit quality by assignment of an NAIC Designation shall be further expanded into NAIC Designation Categories as, and for the purposes, discussed in this Manual.~~

    ~~**NOTE**: See "Production of NAIC Designations" in Part Two.~~

~~Other Non-Payment Risk in Securities~~

~~39. The result of the SVO's analysis of securities for other non-payment risk is expressed by the assignment of an NAIC Designation Subscript S and the application of the notching procedures described below.~~

> ~~**NOTE**: See "NAIC Designation Subscript S" and "SVO Notching Guidelines" in Part Two.~~

NAIC DESIGNATIONS

Regulatory Objective

88. An objective of the VOS/TF is to support regulators in the assessment of the financial ability of an insurer to maintain financial solvency, ~~pay claims~~ through the making of policy concerning insurer investment risk and the identification and sharing of pertinent information with other relevant regulators and regulatory groups responsible for the NAIC's regulatory framework. ~~For example, the regulatory assumption is that a fixed income instrument called debt by its originator or issuer requires that the issuer make scheduled payments of interest and fully repay the principal amount to the insurer on a date certain. A contractual modification that is inconsistent with this assumption creates a rebuttable inference that the security or instrument contains an additional or other non-payment risk created by the contract that may result in the insurer not being paid in accordance with the underlying regulatory assumption. NAIC Designations are required to reflect such contractual modifications and quantify the possibility that such contracts will result in a diminution in payment to the insurer.~~

Definitions

89. NAIC Designations represent opinions of gradations ~~credit quality~~ of the likelihood of an insurer's timely receipt of an investment's full principal and expected interest. Where appropriate for a given investment, NAIC Designations and Designation Categories shall reflect "tail risk" and/or loss given default, ~~. NAIC Designations and Designations Categories shall reflect~~ the position of the specific liability in the issuer's capital structure, ~~and other non-payment risks or non-payment mitigants. NAIC Designations do not measure~~ and all other risks ~~or factors that may affect repayment, such as~~, except for volatility/interest rate, prepayment, extension or liquidity risk. *[Editing Note: moved from Part One, para. 37]* NAIC Designations shall be identified by the NAIC 1 through NAIC 6 symbols (as modified by NAIC Designation Categories) which indicate the highest quality (least risk) to the lowest quality (greatest risk), respectively~~, and which reflect the likelihood of timely and full payment of principal and scheduled periodic interest, in accordance with the regulatory objectives explained above, and the likelihood of principal and/or interest payment default~~.

Use and Purposes of NAIC Designations

90. **NAIC Designations** are proprietary symbols of the NAIC. The SVO, the SSG and, under certain circumstances, insurers, produce NAIC Designations for insurer-owned securities using the policies, procedures or methodologies adopted by the VOS/TF in this Manual. *[Editing Note: Moved from Part Two, para. 18.]* The ~~credit~~ analysis is performed solely for the

purpose of designating the quality of an investment made by an insurance company so that the NAIC member's department of insurance can better identify regulatory treatment. *[Editing Note: moved from Part One, para. 37]* ~~Credit~~ Investment risk is assessed by analyzing the information and documentation provided to the SVO by the reporting insurance company and its advisors. The SVO does not audit the information submitted and assumes the information to be timely, accurate and reliable. *[Editing Note: moved from Part One, para. 37]*

91. **NAIC Designations** are produced for statutory accounting, reporting, state investment laws and other purposes identified in the NAIC Financial Regulation Standards and Accreditation Program and/or other NAIC developed regulatory guidance embodied in state law *[Editing note: Moved from Part Two, para. 18]* and must be interpreted by the NAIC member in context of the NAIC Financial Regulation Standards and Accreditation Program, other characteristics of the investment, and the specific financial and regulatory status of the insurance company. *[Editing note: Moved from Part One, para. 37]* ~~NAIC Designations are adjusted in accordance with the notching procedures described below so that an NAIC Designation for a given security reflects the position of that specific security in the issuer's capital structure. NAIC Designations may also be adjusted by notching to reflect the existence of other non-payment risk in the specific security in accordance with the procedures described in this Manual.~~ *[Editing note: Deleted from Part Two, para. 18]*

92. **NAIC Designations** must be considered in the context of its appropriateness and consistency of use in the NAIC Policy Statement and Financial Regulation Standards (SFRS) and other NAIC guidance. For example, the NAIC Designation serves as the basis for determining the appropriate risk-based capital ~~charge~~ factor for a given security. NAIC Designations should consider if risks, such as tail-risk, are inconsistent with, or duplicative of, risks already captured and defined in the risk-based capital factors, as applicable.

93. ~~**NAIC Designation** – Means any one of the gradations of credit quality and credit risk identified by the **NAIC 1** through **NAIC 6** symbols further discussed and defined in this Manual and may reflect notching pursuant to one or both of the notching procedures discussed in this Manual. NAIC Designations are proprietary symbols of the NAIC to be used by the SVO and SSG or under certain circumstances by an insurer to denote a category or band of credit risk.~~
[Editing note: Originally in Part One, para. 88]

APPLICATION OF NAIC DESIGNATIONS

94. **NAIC 1** is assigned to obligations exhibiting the highest quality. ~~Credit~~ Investment risk is at its lowest and the issuer's credit profile is stable. This means that interest, principal or both will be paid in accordance with the contractual agreement and that repayment of principal is well protected. An **NAIC 1** obligation should be eligible for the most favorable treatment provided under the NAIC Financial Regulation Standards and Accreditation Program.
[Editing note: Moved from Part Two, para. 19]

95. **NAIC 2** is assigned to obligations of high quality. ~~Credit~~ Investment risk is low but may increase in the intermediate future and the issuer's credit profile is reasonably stable. This means that for the present, the obligation's protective elements suggest a high likelihood that interest, principal or both will be paid in accordance with the contractual agreement, but there are suggestions that an adverse change in circumstances or economic, financial or business conditions will affect the degree of protection and lead to a weakened capacity to pay. An **NAIC 2** obligation should be eligible for relatively favorable treatment under the NAIC Financial Regulation Standards and Accreditation Program.
[Editing note: Moved from Part Two, para. 20]

96. **NAIC 3** is assigned to obligations of medium quality. ~~Credit~~ Investment risk is intermediate and the issuer's credit profile has elements of instability. These obligations exhibit speculative elements. This means that the likelihood that interest, principal or both will be paid in accordance with the contractual agreement is reasonable for the present, but an exposure to an adverse change in circumstances or economic, financial or business conditions would create an uncertainty about the issuer's capacity to make timely payments. An **NAIC 3** obligation should be eligible for less favorable treatment under the NAIC Financial Regulation Standards and Accreditation Program.
[Editing note: Moved from Part Two, para. 21]

97. **NAIC 4** is assigned to obligations of low quality. ~~Credit~~ Investment risk is high and the issuer's credit profile is volatile. These obligations are highly speculative, but currently the issuer has the capacity to meet its obligations. This means that the likelihood that interest, principal or both will be paid in accordance with the contractual agreement is low and that an adverse change in circumstances or business, financial or economic conditions would accelerate credit risk, leading to a significant impairment in the issuer's capacity to make timely payments. An **NAIC 4** obligation should be accorded stringent treatment under the NAIC Financial Regulation Standards and Accreditation Program.
[Editing note: Moved from Part Two, para. 22]

98. **NAIC 5** is assigned to obligations of the lowest credit quality, which are not in or near default. ~~Credit~~ Investment risk is at its highest and the issuer's credit profile is highly volatile, but currently the issuer has the capacity to meet its obligations. This means that the likelihood that interest, principal or both will be paid in accordance with the contractual agreement is significantly impaired given any adverse business, financial or economic conditions. An **NAIC 5** Designation suggests a very high probability of default. An **NAIC 5** obligation should incur more stringent treatment under the NAIC Financial Regulation Standards and Accreditation Program.
[Editing note: Moved from Part Two, para. 23]

99. **NAIC 6** is assigned to obligations that are in or near default. This means that payment of interest, principal or both is not being made, or will not be made, in accordance with the contractual agreement. An **NAIC 6** obligation should incur the most severe treatment under the NAIC Financial Regulation Standards and Accreditation Program. *[Editing note: Moved from Part Two, para. 24]*

NOTE: See ~~"NAIC Designations,"~~ "Prohibition on Use of NAIC Designation in a Covenant" and "Coordination Between the Statutory Accounting Principles Working Group and the Valuation of Securities Task Force" in Part One; ~~"NAIC Designation Categories" below~~; and "Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities" in Part Three.

APPLICATION OF NAIC DESIGNATION CATEGORIES

100. Upon the determination of an NAIC Designation, the SVO produces NAIC Designation Categories~~, as described and defined in this Manual~~.
[Editing note: Moved from Part Two, para. 25]

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

~~**NOTE:** See "Production of NAIC Designations" in Part Two.~~
[Editing Note: Moved from Part One, para. 89.]

102. **NAIC Designation Categories** are a subset of **NAIC Designations** and are used by the VOS/TF to link the NAIC risk-based-capital (RBC) framework adopted by the NAIC Capital Adequacy (E) Task Force to the VOS/TF's ~~credit~~ investment risk assessment process. The NAIC Capital Adequacy (E) Task Force assigns RBC factors to each NAIC Designation Category as shown below.

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

[Editing note: Moved from Part Two, para. 26]

103. NAIC Designations and Designation Categories may be adjusted in accordance with the ~~notching~~ procedures described in this Manual ~~below~~ so that an NAIC Designation and Designation Category for a given security reflects the position of that specific security in the issuer's capital structure~~, and other non-payment risks or non-payment mitigants~~. ~~NAIC Designations may also be adjusted by notching to reflect the existence of other non-payment risks in the specific security in accordance with the procedures described in this Manual associated with NAIC Designations Subscript S.~~
[Editing note: Moved from Part Two, para. 18]

NAIC DESIGNATIONS RELATED TO SPECIAL REPORTING INSTRUCTION

104. 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~~ investment risk 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*.
[Editing note: Moved from Part Two, para. 27]

105. 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. *[Editing note: Moved from Part Two, para. 28]*

106. Securities with NAIC 5GI Designations are deemed to possess the ~~credit~~ investment risk 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. *[Editing note: Moved from Part Two, para. 29]*

107. 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. *[Editing note: Moved from Part Two, para. 30]*

108. Securities with NAIC 6* Designations are deemed to possess the credit investment risk 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. *[Editing note: Moved from Part Two, para. 31]*

109. 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.

[Editing note: Moved from Part Two, para. 32]

~~**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.
[Editing note: Moved from Part Two, para. 32]

NAIC General Interrogatory

110. **NAIC 5GI** and NAIC Designation Category **NAIC 5.B GI** is assigned by an insurance company to certain obligations that meet all of the following criteria:

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

[Editing note: Moved from Part One, para. 91]

NAIC PLGI

111. Effective July 1, 2018, insurance companies shall be responsible for providing the SVO copies of private rating letters for PL securities, where applicable, until such time as industry representatives and the SVO shall have established reliable procedures for obtaining the necessary information on credit ratings directly from the NAIC CRPs. For PL Securities issued prior to January 1, 2018, if an insurance company cannot provide a copy of the rating letter to the SVO due to confidentiality concerns and the rating is not included in a CRP credit rating feed (or other form of direct delivery from the NAIC CRP), the insurer shall report such securities on such securities' General Interrogatory to be developed for this purpose (i.e., a PLGI security).
[Editing note: Moved from Part One, para. 92]

Monitoring of SVO-Designated Securities

112. The SVO shall monitor, on an ongoing basis through the information provided by insurers as required by the Material Credit Events Filing described in this Manual, improvements and deterioration of credit quality of securities that are not filing exempt.
[Editing note: Moved from Part One, para. 93]

PART TWO
OPERATIONAL AND ADMINISTRATIVE INSTRUCTIONS
APPLICABLE TO THE SVO

~~PRODUCTION OF NAIC DESIGNATIONS~~ [EDITING NOTE: MOVED TO PART ONE "NAIC DESIGNATIONS".]

~~NAIC DESIGNATIONS~~

~~18. NAIC Designations are proprietary symbols of the NAIC. The SVO and sometimes the SSG produce NAIC Designations for insurer-owned securities using the policies, procedures or methodologies adopted by the VOS/TF in this Manual. NAIC Designations identify a category or band of credit risk. NAIC Designations are produced for statutory accounting, reporting, state investment laws and other purposes identified in the NAIC Financial Regulation Standards and Accreditation Program and/or other NAIC developed regulatory guidance embodied in state law. NAIC Designations are adjusted in accordance with the notching procedures described below so that an NAIC Designation for a given security reflects the position of that specific security in the issuer's capital structure. NAIC Designations may also be adjusted by notching to reflect the existence of other non-payment risk in the specific security in accordance with the procedures described in this Manual.~~

~~19. **NAIC 1** is assigned to obligations exhibiting the highest quality. Credit risk is at its lowest and the issuer's credit profile is stable. This means that interest, principal or both will be paid in accordance with the contractual agreement and that repayment of principal is well protected. An **NAIC 1** obligation should be eligible for the most favorable treatment provided under the NAIC Financial Regulation Standards and Accreditation Program.~~

~~20. **NAIC 2** is assigned to obligations of high quality. Credit risk is low but may increase in the intermediate future and the issuer's credit profile is reasonably stable. This means that for the present, the obligation's protective elements suggest a high likelihood that interest, principal or both will be paid in accordance with the contractual agreement, but there are suggestions that an adverse change in circumstances or economic, financial or business conditions will affect the degree of protection and lead to a weakened capacity to pay. An **NAIC 2** obligation should be eligible for relatively favorable treatment under the NAIC Financial Regulation Standards and Accreditation Program.~~

~~21. **NAIC 3** is assigned to obligations of medium quality. Credit risk is intermediate and the issuer's credit profile has elements of instability. These obligations exhibit speculative elements. This means that the likelihood that interest, principal or both will be paid in accordance with the contractual agreement is reasonable for the present, but an exposure to an adverse change in circumstances or economic, financial or business conditions would create an uncertainty about the issuer's capacity to make timely payments. An **NAIC 3** obligation should be eligible for less favorable treatment under the NAIC Financial Regulation Standards and Accreditation Program.~~

~~22. **NAIC 4** is assigned to obligations of low quality. Credit risk is high and the issuer's credit profile is volatile. These obligations are highly speculative, but currently the issuer has the capacity to meet its obligations. This means that the likelihood that interest, principal or both will be paid in accordance with the contractual agreement is low and that an adverse change in circumstances or business, financial or economic conditions would accelerate credit risk, leading to a significant impairment in the issuer's capacity to make timely payments. An **NAIC 4** obligation should be accorded stringent treatment under the NAIC Financial Regulation Standards and Accreditation Program.~~

~~23. **NAIC 5** is assigned to obligations of the lowest credit quality, which are not in or near default. Credit risk is at its highest and the issuer's credit profile is highly volatile, but currently the issuer has the capacity to meet its obligations. This means that the likelihood that interest, principal or both will be paid in accordance with the contractual agreement is significantly impaired given any adverse business, financial or economic conditions. An **NAIC 5** Designation suggests a very high probability of default. An **NAIC 5** obligation should incur more stringent treatment under the NAIC Financial Regulation Standards and Accreditation Program.~~

~~24. **NAIC 6** is assigned to obligations that are in or near default. This means that payment of interest, principal or both is not being made, or will not be made, in accordance with the contractual agreement. An **NAIC 6** obligation should incur the most severe treatment under the NAIC Financial Regulation Standards and Accreditation Program.~~

~~**NOTE**: See "NAIC Designations," "Prohibition on Use of NAIC Designation in a Covenant" and "Coordination Between the Statutory Accounting Principles Working Group and the Valuation of Securities Task Force" in Part One; "NAIC Designation Categories" below; and "Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities" in Part Three.~~

~~NAIC DESIGNATION CATEGORIES~~

~~25. Upon the determination of an NAIC Designation, the SVO produces NAIC Designation Categories, as described and defined in this Manual.~~

~~26. NAIC Designation Categories are a subset of NAIC Designations and are used by the VOS/TF to link the NAIC risk-based-capital (RBC) framework adopted by the NAIC Capital Adequacy (E) Task Force to the VOS/TF's credit assessment process. The NAIC Capital Adequacy (E) Task Force assigns RBC factors to each NAIC Designation Category as shown below.~~

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

~~NAIC DESIGNATIONS RELATED TO SPECIAL REPORTING INSTRUCTION~~

~~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.~~

~~NAIC DESIGNATION SUBSCRIPT S~~

~~**Description of Other Non-Payment Risk**~~

~~33. It may not be practical, desirable or possible to specifically define other non-payment risk given the assumption that it originates as a result of a contractual agreement or the presence of a structural element of a transaction that is agreed upon between the issuer and the insurer. Accordingly, what follows is intended as general guidance to insurers and others.~~

~~34. Most typically, other non-payment risk has been associated with contractual agreements between the insurer and the issuer in which the issuer is given some measure of financial flexibility not to make payments that otherwise would be assumed to be scheduled, given how the instrument has been denominated, or the insurer agrees to be exposed to a participatory risk.~~

~~35. Other non-payment risk differs from the type of issues encountered in credit risk. This is because typically, credit assessment is concerned with securities in which the parties create subordination by modifying the lender's priority of payment (e.g., senior unsecured versus junior subordinated) but in a context where the contract otherwise specifies that the failure to make payments on a schedules basis (defined in the contract) is an event of default (in the case of a bond) or triggers some other specific and identifiable lender remedy (in the case of other fixed income securities).~~

~~36. Using the broad concepts identified above, non-payment risk may be present when:~~

- ~~A reporting insurance company takes on a participatory risk in the transaction;~~

  ~~*Illustration – The contract promised payment of a dollar denominated obligation in non-U.S. currency but does not require an exchange rate that would yield foreign currency sufficient to buy a defined principal amount of U.S. dollars. The other non-payment risk in this illustration consists of the reporting insurance company's acceptance of currency risk which may diminish the principal amount of the investment. Currency risk here is not related to the issuer's ability or willingness to pay and therefore is not appropriately reflected in the NAIC Designation of the issuer or captured by notching for credit risk.*~~

- ~~The contract governing the loan provides for a degree of permanence in the borrower's capital structure that is incompatible with notions of a loan that is expected to be repaid;~~

  ~~*Illustration – A loan stated to be perpetual and giving the issuer the right to miss interest or dividend payments otherwise said to be scheduled where the missed payments are not required to be paid on a subsequent date.*~~

  ~~*Illustration – An instrument denominated as a bond but lacking a maturity date, a mechanism to determine a maturity dates (e.g., a mandatory redemption) or that states a maturity equal to*~~

~~*or exceeding 40 years*~~.

~~37. Agrees to an exposure that has the potential to result in a significant delay in payment of contractually promised interest and/or a return of principal in an amount less than the original investment.~~

~~Meaning of the Subscript S Symbol~~

~~38. An SVO determination that a specific security contains other non-payment risk is communicated by assigning the NAIC Designation subscript S to the specific CUSIP and applying the notching procedure described below. The subscript follows the NAIC Designation as follows:~~ **~~NAIC 2S~~**~~.~~

~~39. The SVO shall assess securities for other non-payment risk:~~

- ~~Routinely, for any security or financial product filed with the SVO.~~
- ~~As part of the analysis of a security or financial product submitted to the SVO under the RTAS – Emerging Investment Vehicle process discussed in of this Manual.~~
- ~~When requested to do so by any state insurance regulator acting pursuant to this Manual, and:~~

  ~~When requested by the VOS/TF; or~~

  ~~In support of any other NAIC group engaged in the analysis of investment risks in new securities.~~

~~**NOTE**: See "NAIC Designation Subscript S" in Part One.~~

NAIC NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

Attachment G
Valuation of Securities (E) Task Force
6/18/2024

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

RE: Revised Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (the "P&P Manual") Authorizing the Procedures for the SVO's Discretion Over NAIC Designations Assigned Through the Filing Exemption Process

DATE: June 4, 2024

Summary: At the Summer National Meeting held on Aug. 14, 2023, the Task Force discussed an initial draft of a proposed amendment to the P&P Manual authorizing the procedures for the SVO's discretion over NAIC designations assigned through the filing exemption (FE) process. The Task Force directed the SVO staff to consider the feedback from Task Force members and interested parties and update the proposal. At the subsequent Spring National Meeting held on March 16, 2024, the Task Force received additional comments on the updated amendment. The revised amendment in this memorandum reflects the recommended actionable comments received from Task Force members and interested parties during each comment period.

The revised amendment incorporates the following process steps, many of which were requested by interested parties:

1) SVO staff identifies a FE security with an NAIC Designation determined by a rating that appears to be an unreasonable assessment of investment risk.
2) SVO Credit Committee (CC) meets to determine if it agrees that the rating appears to be an unreasonable assessment of investment risk and, if so, places the security "Under Review".
3) If the SVO CC votes to put the security "Under Review", an information request will be sent through VISION to insurers that hold that security in their VISION portfolio and statutory financial statements, and the SVO Administrative Symbol "UR" will be assigned to identify them in VISION and AVS+.
4) If the information request is not responded to, the SVO may reach out to the domiciliary chief financial regulator.
5) Upon receipt of all necessary documentation through the information request, the SVO will then perform a full analysis of the security. During it's the review the SVO will coordinate with insurer(s) authorized to discuss the security to discuss questions or issues the SVO may have about the security and to respond to any questions the authorized

insurer(s) staff may have about the SVO's analysis. This communication is intended to be an open dialogue.

6) The SVO CC re-convenes to determine, based on its full analysis of all necessary information, whether the FE NAIC Designation is three (3) or more notches different than the SVO CC's opinion and, therefore, whether the SVO should proceed in requesting the removal of the CRP Rating from the FE process.
7) If the SVO CC's decision is to proceed with the CRP rating removal request, the SVO CC and a Sub-group of the Task Force will meet to discuss the security. The domiciliary regulators of the authorized insurers will be invited to the Task Force Sub-group meeting and provided with relevant documentation through a confidential website. The authorized insurer(s) staff and other authorized parties requested by those insurers to participate, will be invited to present their analysis to the joint meeting. Also at that meeting, the SVO CC will present its analysis, which may include any information provided to it or independently sourced. Following the presentations, the SVO CC and Task Force Sub-group will deliberate privately and the Task Force Sub-Group will vote on whether it agrees with the SVO CC recommendation and whether the CRP rating will be removed from the FE process. At the conclusion of the joint meeting, the IAO will communicate the decision to the authorized insurer(s).
8) At any time during this process an alternate CRP rating may be requested. If an alternative CRP rating is received, it will be incorporated into the FE process, if applicable. If there are no alternative CRP ratings, the SVO CC's assessment will be entered into VISION if the Task Force Sub-group approves the CRP rating removal.
9) An anonymized summary of each unique issue or situation will be published on the SVO webpage or some other insurer accessible location for transparency.
10) The SVO will identify through SVO Administrative Symbols when a CRP rating(s) has been removed from the Filing Exemption process for a security.
11) At the Spring National Meeting, the SVO Director will summarize FE discretion actions taken during the preceding year.

Recommendation: It is expected that implementation of this process will require enhancements to NAIC's VISION and AVS+ applications. Additionally, given the requested revisions in this proposal to potentially share highly confidential and material non-public information, it may be necessary for the NAIC to add compliance and analytical review staff, and use specialized commercial systems to ensure confidentiality. Funding for the application enhancements, staffing and other system needs in the amendment, will need to be approved by the Executive (EX) Committee and the initiative will need to go through the NAIC's development and procurement process. It could take 1-2 years before this proposal can be fully implemented and fees will likely be needed to recover the initial and ongoing expense related to the revised proposal.

The SVO recommends adoption of this proposed amendment authorizing the procedures for the SVO's discretion over NAIC Designations assigned through the FE process with an effective date of January 1, 2026. The effective date can be amended, if needed, because of the dependency mentioned. The proposed text changes to P&P Manual are shown below with additions in red underline, and deletions in ~~red strikethrough~~ as it would appear in the 2023 P&P Manual format.

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

…

POLICIES APPLICABLE TO THE FILING EXEMPTION (FE) PROCESS

NOTE: The policies below provide the policy framework for "Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities" in Part Three and are related to "The Use of Credit Ratings of NRSROs in NAIC Processes" discussed above; "NAIC Policy on the Use of Credit Ratings of NRSROs" and the "Definition – Credit Ratings Eligible for Translation to NAIC Designations" in Part Two ("Eligible NAIC CRP Credit Ratings" excludes the use of any credit rating assigned to a security type where the NAIC has determined that the security type is not eligible to be reported on Schedule D or the it is not appropriate for NRSRO credit ratings to be used to determine the regulatory treatment of the security or asset.)

Determinations

80. The VOS/TF is resolved that the benefit obtained from the use of credit ratings in state regulation of insurance (i.e. conservation of limited regulatory resources) must be balanced against the risk of blind reliance on credit ratings. To ensure the Task Force properly understands the composition and risk of the filing exempt securities population~~;~~, promote uniformity in the production of NAIC Designations, reduce reporting exceptions for filing exempt securities and increase the efficiency of this NAIC process, the SVO and SSG (hereafter, the IAO) is charged with administration of the filing exempt process defined in Part Three of this Manual.

Directives

81. The IAO shall:

- Recommend improvements to the production of NAIC Designations based on NRSRO credit ratings.
- Identify monitoring and communication procedures that enhance the possibility of regulatory intervention by the VOS/TF to respond to risks to insurer solvency posed by securities in the filing exempt population.
- Identify and develop correctives to the administrative, operational and system-based causes of reporting exemptions in the filing exempt process.

- Change the NAIC Designation equivalent calculated for filing exempt securities when necessary to correct errors or other anomaly that occur in the automated filing exempt process.
- Develop a staff-administered reporting exceptions resolution process that incorporates state insurance regulator and insurance companies' participation.
- In furtherance of the above directives, exclude specific otherwise Eligible NAIC CRP Credit Ratings from the automated filing exemption process in accordance with the administrative procedures outlined in Part Two of this Manual, if a Sub-group of the Task Force agrees with the determination of the IAO Credit Committee that the resulting NAIC Designation equivalent does not provide a reasonable assessment of investment risk for regulatory purposes.

...

PART TWO
OPERATIONAL AND ADMINISTRATIVE INSTRUCTIONS
APPLICABLE TO THE SVO

SVO ORGANIZATION

…

SVO Administrative Symbols

153. SVO administrative symbols convey information about a security or an administrative procedure instead of an opinion of credit quality. The administrative symbols in use by the SVO and their meanings are described below.

SVO Analytical Department Symbols

154. All SVO analytical departments use the following administrative symbols:
…

- **UR** means the NAIC Designation assigned pursuant to the filing exemption process is under review by the NAIC's Investment Analysis Office.
- **ER** means that one or more otherwise Eligible NAIC CRP Credit Ratings have been excluded from the filing exemption process when determining the NAIC Designation through the Eligible NAIC CRP Rating exclusion procedures in this Manual.

PROCESS FOR EXCLUDING AN ELIGIBLE NAIC CRP RATING FROM FILING EXEMPTION FOR A SPECIFIC SECURITY

Overview

164. This section outlines the process by which a state insurance regulator or IAO staff can contest an NAIC Designation Category assigned through the filing exemption process which it thinks is not a reasonable assessment of investment risk of the security for regulatory purposes. **(Note: The guidance in this part is effective as of January 1, 2026, but this date may be amended if additional time is needed to implement the necessary NAIC technological enhancements to IAO systems.)**

Request for Information

165. The IAO staff will bring to the attention of the Credit Committee any filing exemption-eligible security assigned an NAIC Designation Category equivalent through the automated filing exemption process as being a security under review if (i) a state insurance regulator notifies the IAO staff that it has determined the NAIC Designation Category equivalent may not be a reasonable assessment of investment risk of the security for regulatory purposes, or (ii) the IAO staff, in its opinion, determines that the NAIC Designation Category equivalent may not be a reasonable assessment of investment risk of the security for regulatory purposes. State insurance regulator notification pursuant to this section does not negate the authority of state insurance regulators under "States May Require a Filing of Exempt or Other Transactions" in Part One of this Manual.

166. The Credit Committee will convene to determine if, in its opinion, the NAIC Designation Category assigned pursuant to the filing exemption process is a reasonable assessment of investment risk of the security for regulatory purposes. As part of its review, the Credit Committee may consider observable factors including, but not limited to (i) a comparison to peers rated by different CRPs, (ii) consistency of the security's yield at issuance or current market yield to securities with equivalently calculated NAIC Designations rated by different CRPs, (iii) the IAO's assessment of the security applying available methodologies, and (iv) any other factors it deems relevant. If the Credit Committee's opinion is that the assigned NAIC Designation Category is likely a reasonable assessment of investment risk of the security for regulatory purposes, no further action will be taken at that time. If the Credit Committee's opinion is that the assigned NAIC Designation Category is likely not a reasonable assessment of investment risk of the security for regulatory purposes, an information request will be initiated and the security will be put under review.

167. The IAO will notify insurance company holders of the security determined to be a Filing Exempt Security "Under Review" by issuing an information request and publishing a separate SVO Analytical Department Symbol of "UR" for under review in NAIC systems. The SVO Analytical Department Symbol of "UR" will not be reported on the statutory investment schedules. The purpose of the information request is to notify insurance company holders of the security to provide the IAO staff with sufficient information to perform a full analysis of the security. The information provided by insurers should be comparable to an Initial Filing, as described in this Manual, and must be accompanied by each insurer's internal analysis. Consistent with the informational deficiency instructions in this Manual, security information consistent with an Initial Filing should be provided to the IAO within 45 days unless an extension has been granted to the insurance company by the IAO, not to exceed 90 days in total from the date that the IAO issues an information request. The IAO may contact the insurance company's domiciliary chief financial regulator for assistance after the initial 45 days if there has been no meaningful response. If after 90 days additional information equivalent to an Initial Filing has not been provided to the IAO, the IAO may proceed with removal of the otherwise Eligible NAIC CRP Credit Rating(s) from the Filing Exempt process without convening the Sub-group of the Task Force, as described in this section.

Full Review

168. At any time during the information request submission period or during the IAO's subsequent analysis of the security, the insurance company holders of the security are encouraged to provide additional information to the IAO such as their internal analysis, presentations from the issuer, meetings with the issuer's management team and any other information that may be useful or persuasive in the analysis of the security. The IAO will coordinate with the authorized insurer(s) staff to discuss any questions or issues the IAO may have about the security and answer any question that the authorized insurer(s) staff may have about the IAO's analysis.

169. Upon satisfactory receipt of the information through the information request, the IAO will perform a full analysis of the security during which time the SVO Analytical Department Symbol "UR" will remain in place but this symbol will not be reported on the statutory investment schedules.

IAO Determination and Materiality Threshold

170. Upon completion of the IAO's analysis, the Credit Committee will reconvene to determine its own opinion of the NAIC Designation Category. The Credit Committee will then determine whether the NAIC Designation Category assigned through the automated filing exemption process is materially different from its own assessment of the security's risk.

171. The IAO will consider the materiality of the difference between the Eligible NAIC CRP Credit Rating used in the filing exempt process and the IAO's own assessment of the risk. The IAO may propose the removal of an otherwise Eligible NAIC CRP Credit Rating from the Filing Exemption process to a Task Force Sub-group only if the Credit Committee determines, based upon its review, that the Eligible NAIC CRP Credit Rating for the security is three (3) or more notches different than the IAO's assessment (e.g. NAIC Designation Category 1.G versus 2.C) (the "Materiality Threshold").

Valuation of Securities (E) Task Force Oversight

172. The Credit Committee shall schedule a call with a VOS/TF Sub-Group (the composition of which shall be determined by the VOS/TF chair), for so long as the VOS/TF chair deems such meetings necessary, to discuss and explain its analytical basis for any Eligible NAIC CRP Credit Rating being recommended for removal from Filing Exemption eligibility. The Credit Committee will use communication processes that maintain confidentiality and notify domiciliary regulators of insurer holders of the security of the Sub-group meeting.

173. If the Credit Committee identifies that there is a recurring analytical pattern or concern, the IAO Director(s) will inform the VOS/TF chair and they will decide if an issue paper, referral, amendment to this Manual or some other action is needed.

174. Insurance company staff, and other parties invited by the insurer, that are authorized to discuss the security and who have agreed to confidentiality provisions required by the NAIC, may present their analytical basis to maintain the Eligible NAIC CRP Credit Rating's eligibility for Filing Exemption to the joint meeting of the VOS/TF Sub-group and the Credit Committee. Any materials shared during this meeting with the VOS/TF Sub- and Credit Committee are considered highly confidential and may not be shared beyond those participants at the meeting that have been identified as having been authorized to receive such materials and have agreed to maintain their confidentiality.

175. If, at any time, the VOS/TF chair chooses not to convene a VOS/TF Sub-Group for this process, then the Credit Committee will conduct the meeting with insurance company staff and other invited parties without a VOS/TF Sub-Group and the Credit Committee's decision following such meeting will stand.

Assignment of NAIC Designation Category

176. If the VOS/TF Sub-group disagrees with the Credit Committees' NAIC Designation Category opinion and determines that the NAIC Designation Category assigned pursuant to the Filing Exemption process *does not* meet the Materiality Threshold, the Eligible NAIC CRP Credit Rating shall remain eligible for Filing Exemption, the SVO Analytical Department Symbol "UR" will be deactivated, and no further action will be taken at that time. This determination shall not preclude the IAO from placing the same Eligible NAIC CRP Credit Rating under analytic review at a later date following a subsequent review should changing conditions warrant.

177. If the VOS/TF Sub-group agrees with the Credit Committees' NAIC Designation Category opinion and determines that the NAIC Designation Category assigned pursuant to the Filing Exemption process *does* meet the Materiality Threshold, the IAO is authorized to block the otherwise Eligible NAIC CRP Credit Rating in NAIC systems to prevent that otherwise Eligible NAIC CRP Credit Rating from being used in the automated Filing Exempt Securities Process.

178. If an Eligible NAIC CRP Rating has been removed from Filing Exemption eligibility for a security according to this section and the security has other Eligible NAIC CRP Rating(s) which have not been removed or the security receives an additional Eligible NAIC CRP Rating at any time during or after this process, then the security can receive its NAIC Designation Category through the Filing Exemption process based on the Eligible NAIC CRP Rating(s) that have not been removed. If there is no alternate Eligible NAIC CRP Rating in NAIC systems, the Credit Committee's NAIC Designation Category will be entered into NAIC systems to assign an NAIC Designation Category to the security.

Reinstatement of Filing Exemption Eligibility

179. If an insurer would like the IAO to re-evaluate an Eligible NAIC CRP Credit Rating that was removed from Filing Exemption Eligibility for possible reinstatement in a subsequent filing year, it can follow the operational steps outlined in Appeals of SVO Determinations in this Manual to submit the request.

Reporting Securities Removed from Filing Exemption Eligibility

180. The IAO Director(s) will prepare a summary of the removed from Filing Exemption Eligibility actions take over the prior calendar year.

181. The IAO will also publish an anonymized summary of each unique situation encountered for the securities subject to removal from Filing Exemption Eligibility and publish it on an insurer accessible web location.

182. To facilitate transparency as to the SVO's application of discretion, the SVO Analytical Department Symbols "ER' will be added in NAIC Systems to securities with an excluded otherwise Eligible NAIC CRP Credit Rating(s). The SVO Analytical Department Symbols, "ER" *will be* reported on the insurer's statutory investment schedules for the effected security instead of SVO Administrative Symbols "FE" for filing exemption.

…

C:\Users\CTherriault\OneDrive - National Association of Insurance Commissioners\Documents - SVO - VOS Task Force\Meetings\2024\2024-06-18 VOSTF Interim Meeting\02-SVO Discretion\2023-005.15 P&P SVO Discretion - Revised v5.docx