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**MEMORANDUM**

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

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

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

RE: Proposed Amendment to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* (P&P Manual) to Clarify That the Sovereign Rating Limitation Applies to Filing Exemption (FE)

DATE: September 30, 2019

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**1. Introduction** – The P&P Manual has criteria capping the NAIC Designation that the SVO can assign to a foreign security to the sovereign rating of the issuer’s country of origin. This sovereign limitation is not currently explicitly addressed when an NAIC Designation is produced through the filing exempt instructions. This proposed amendment provides that consistency by limiting all NAIC Designations for foreign securities to the NAIC’s Foreign Sovereign Designation Equivalent list published on the SVO’s webpage.

**2. Proposed Amendment** – The text referencing the NAIC Designation cap for foreign securities is shown below, edits in red-underline, as it will appear in the 2019 P&P Manual format.

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**2019 P&P Manual**

**Part One – Policies of the NAIC Valuation of Securities (E) Task Force**

**Special Instructions**

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**Sub-paragraph D Company**

121. The insurance company must file all foreign securities for which the information required by this Manual is available. For those foreign securities held by a “Sub-paragraph D Company” as defined below, where the required information is not available for the SVO to value the security, the NAIC Designation may be determined by the reporting insurance company. This determination shall carry an **F** suffix. In no case shall the NAIC Designation exceed the sovereign rating of the issuer’s country of origin as published in the NAIC’s Foreign Sovereign Designation Equivalent list on the SVO’s webpage. The company shall provide its domestic regulator with a description of the procedure it used to evaluate and assign ratings to these foreign securities. In addition, the company shall retain the documentation supporting each designation assigned by it until the next domestic insurance department examination.

**Part Three – SVO Procedures and Methodology for Production of NAIC Designations**

**List of NAIC Credit Rating Providers**

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<b>LIMITATIONS ON USE OF NAIC CRP RATINGS</b>
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**NAIC Designation is Capped to NAIC Foreign Sovereign Designation Equivalent**

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28. The NAIC shall not assign an NAIC Designation for any foreign security which qualifies as a foreign investment as defined in the Annual Statement Instructions published by the NAIC, whether or not eligible for filing exemption, that is greater than the sovereign rating of the issuer’s country of origin indicated by the NAIC Foreign Sovereign Designation Equivalent listed on the SVO’s webpage.

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**Part Three – SVO Procedures and Methodology for Production of NAIC Designations**  
**GENERAL CORPORATE AND MUNICIPAL METHODOLOGY FOR INDEPENDENT CREDIT**  
**QUALITY ASSESSMENT**

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<b>FOREIGN SECURITIES</b>
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**Foreign Sovereign Government, ~~and~~ Supranational Entities and Foreign Securities**

28. A reporting insurance company that owns a security issued by a foreign sovereign government, an agency or political subdivision of a foreign sovereign government or a supranational entity (entities with more than one sovereign government as a member), or that is guaranteed directly or indirectly by such an entity must file such security with the SVO accompanied by a prospectus and investment committee memorandum.
29. Insurance companies shall not file issues with the SVO if the issuer of foreign origin does not have a sovereign rating from an NAIC CRP. If the issuer is not rated by an NAIC CRP, proof of a guarantee from an NAIC CRP-rated foreign sovereign government may be submitted. Where a reporting insurance company has filed a foreign security accompanied by an Audited Financial Statement, in English, the SVO will assess the security in accordance with the applicable corporate methodology, but the NAIC Designation it may assign shall be limited capped by the sovereign rating of the issuer's country of origin. This section should not be read as prohibiting the presentation of transactions structured to eliminate foreign sovereign risk.
30. The insurance company must file all foreign securities for which the information required by this Manual is available. For those foreign securities held by a "Sub-paragraph D Company" as defined in Part One, where the required information is not available for the SVO to value the security, the NAIC Designation may be determined by the reporting insurance company. This determination shall carry an F suffix. In no case shall the NAIC Designation exceed the sovereign rating of the issuer's country of origin. The company shall provide its domestic regulator with a description of the procedure it used to evaluate and assign ratings to these foreign securities. In addition, the company shall retain the documentation supporting each designation assigned by it until the next domestic insurance department examination.
31. The NAIC Designation that can be assigned to a foreign security which qualifies as a foreign investment as defined in the Annual Statement Instructions published by the NAIC, whether or not eligible for filing exemption, shall be capped by the sovereign rating of the issuer's country of origin as published in the NAIC's Foreign Sovereign Designation Equivalent list on the SVO's webpage.

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