



Mike Monahan
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September 21, 2017

Stewart Guerin, Chair
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1100 Walnut Street
Suite 1500
Kansas City, MO 64106-2197

Kevin Fry, Vice Chair
NAIC Valuation of Securities (E) Task Force
1100 Walnut Street
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Kansas City, MO 64016-2197

Re: SVO Report on Fund Investments – A Proposal to Add a Clarifying Instruction to the Purposes and Procedures (P&P) Manual of the NAIC Investment Analysis Office

Dear Messrs. Guerin and Fry:

The American Council of Life Insurers (ACLI)¹ would like to thank the NAIC Valuation of Securities (E) Task Force (VOSTF) for the opportunity to comment and provide input on the staff memorandum related to the SVO's assessment of fund investments, dated February 23, 2017, and exposed by the Valuation of Securities Task Force ("VOSTF") at the Summer National Meeting in Philadelphia.

The memorandum seeks to clarify that fund investments are not filed with the Securities Valuation Office ("SVO") for a NAIC designation and that fund investments are not eligible for filing exemption, except for the specific exceptions recognized in the P&P Manual and the Accounting Practices and Procedures Manual. The three exceptions currently listed in the memorandum are as follows:

- a) Exchange-traded funds ("ETFs"), which qualify for bond or preferred stock treatment, as identified in Part Six, Section 2 of the P&P Manual
- b) Bond mutual funds, which qualify for bond treatment, as identified in Part Six, Section 2, of the P&P Manual
- c) Money market mutual funds on the U.S. Direct Obligations/Full Faith and Credit Exempt List, as identified in Part Six, Section 2 of the P&P Manual

ACLI agrees that mutual funds and ETFs can only be reported as bonds if they have been specifically identified under the P&P Manual in Part Six, Section 2. If an insurer's investment in a mutual fund or ETF

¹ The American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association with approximately 290 member companies operating in the United States and abroad. ACLI advocates in state, federal, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing 95 percent of industry assets, 93 percent of life insurance premiums, and 98 percent of annuity considerations in the United States. Learn more at www.acli.com.

is not listed on the P&P Manual referenced section, such investment should be reported on Schedule D-2-2 as a common stock investment within the scope of the guidance in Statement of Statutory Accounting Principles (“SSAP”) No. 30 - *Investments in Common Stock*, or on Schedule D-2-1 as a preferred stock investment under SSAP No. 32 - *Investments in Preferred Stock*.

Regarding other fund investments reported on Schedule BA, the ACLI strongly believes that there are certain Schedule BA fund investments that can be reported as having underlying investments considered to be fixed income instruments. The P&P Manual states that certain investments reported on Schedule BA may be reported as having fixed income characteristics, as long as the appropriate paperwork is filed with the SVO. If a filing is done with the SVO, the SVO would then provide a NAIC designation so that the investment may be reported in the appropriate section of Schedule BA. This classification allows an insurer to get a less punitive RBC charge than the equity charge to which most Schedule BA investments are subject. Obtaining a NAIC designation on such a fund has nothing to do with accounting and, as such, a fund would still fall under the SSAP 48 accounting provisions. We understood this as merely a mechanism for insurers to get bond-like RBC treatment for bond-like investments, which would otherwise not be allowed if such category did not exist on Schedule BA.

Our understanding of current Schedule BA reporting rules is that if an insurer invests in a private fund set up as either a Limited Liability Company (“LLC”) or a Limited Partnership (“LP”), whose underlying investments are predominantly fixed income instruments such as fixed or floating rate debt securities (or loans), the LLC or LP would qualify for such treatment as follows:

- Investments in private funds set up as either LLCs or LPs, whose underlying investments are comprised predominantly of fixed or floating rate debt securities (or loans), which receive a public rating with annual surveillance from a CRP are reported under the fixed income category on Schedule BA;
- Investments in private funds set up as either LLCs or LPs, for which no public rating is received from a CRP, but whose underlying investments are comprised predominantly of fixed or floating rate debt securities (or loans) rated by a CRP and/or designated by the NAIC, need to be designated by the NAIC in order to be reported under the fixed income category on Schedule BA.

In follow-up discussions with SVO leadership, they have expressed concerns over the lack of instruction/specificity in the P&P Manual regarding these types of investments. To that end, the SVO is receiving complicated transactions from companies which they believe are beyond the scope of the current P&P Manual guidelines. To address this concern and provide additional clarity, ACLI recommends that additional guidance should be added to the P&P Manual. We understand that the SVO prefers a Weighted Average Rating Factor methodology (“WARF”) for evaluation of these investments (referenced in the second bullet above), which we believe the SVO currently uses for other investments. ACLI has no objection to the use of such methodology.

ACLI wants to ensure the retention of our ability to file the aforementioned Schedule BA fund investments that currently qualify for a NAIC designation in accordance with the P&P Manual. We propose the following amendments to be made to the P&P Manual so that the SVO has more definitive guidance on this topic (see bold underlined section below):

Excerpt from the P&P Manual

Part 3, section 5 (b) of the P&P Manual

Fixed Income and Preferred Stock like Schedule BA Assets Defined

The NAIC Financial Statement Blank provides that long-term invested assets that are not clearly or normally includable in any other invested asset schedule are to be reported on Schedule BA of the NAIC Financial Statement Blank. Pursuant to applicable Annual Statement Instructions, a reporting entity determines if a Schedule BA fixed or variable interest rate asset has the underlying characteristics of a bond or other fixed income instrument or that a joint venture, partnership or limited liability company interest has the underlying characteristics of a fixed income instrument. **A Schedule BA fixed or variable rate asset has the underlying characteristics of a bond or other fixed income instrument if it has a stated maturity and a fixed or floating coupon rate. A joint venture, partnership or limited liability company has the underlying characteristics of a fixed income instrument if it predominantly holds debt (or loans) and receives a public rating with annual surveillance from a CRP, or is designated by the NAIC through the application of a Weighted Average Rating Factor ("WARF") methodology that takes into account the NAIC designation and/or the CRP assigned to the underlying investments. Such assets are defined as having the underlying characteristics of a fixed income instrument.** The Annual Statement Instructions provide that a Schedule BA asset with the underlying characteristics of a bond or other fixed income instrument not filed with the SVO must be designated as class six for purposes of calculating an AVR and RBC. In furtherance of the regulatory objectives embodied in the Annual Statement Instructions, this Part provides a procedure through which a reporting entity shall file a Schedule BA asset with the SVO to obtain an NAIC Designation other than NAIC 6 in order to obtain a more favorable AVR. The SVO is hereby charged with responsibility for assigning an NAIC Designation in the circumstances described above, in accordance with subparagraph (e) of this Section.

We thank you for allowing us to comment on this proposal, and we look forward to addressing any questions at your convenience.

Sincerely,



Mike Monahan
Senior Director, Accounting Policy

cc: Charles Therriault, Director, NAIC Securities Valuation Office
Robert Carcano, Sr. Counsel, NAIC Investment Analysis Office