

MEMORANDUM

TO: Dale Bruggeman, Chair, Statutory Accounting Principles (E) Working Group

FROM: Kevin Fry, Chair, Valuation of Securities (E) Task Force

Cc: Charles Therriault, Director, NAIC Securities Valuation Office
Julie Gann, Assistant Director, NAIC Financial Regulatory Services
James Pinegar, Manager II, NAIC Financial Regulatory Services

DATE: January 3, 2020

RE: Referral to the Statutory Accounting Principles (E) Working Group Requesting Comments on P&P Manual Amendment to Rename the U.S. Direct Obligations/Full Faith and Credit Exempt List to the U.S. Government Fund List, and separately Discontinue the Bond Fund List

1. Summary – The P&P Manual authorizes the SVO to maintain two special fund lists. The first is the NAIC U.S. Direct Obligations/Full Faith and Credit Exempt Money Market Funds List. This list of Money Market Funds (MMF) gets special treatment because they can be reported as a cash equivalent on Schedule E, Part 2. The SVO proposed simplifying the title of this list to “NAIC U.S. Government Money Market Fund List.” This is only a proposed title simplification change.

The second list is the NAIC Bond Fund List which is limited to funds that maintain the highest credit quality rating, maintain the highest market risk rating (a rating type that is no longer assigned), and invests 100% of its total assets in U.S. Government securities along with several other restrictive criteria. The SVO reported that only four funds qualify for this list and that four insurers invested in just one of the four qualify funds for a combined exposure of \$11.8 million book adjusted carrying value (BACV) as of December 31, 2018. With the adoption of the Comprehensive Instructions for Fund Investments by the Task Force on April 7th that provides new instructions for Fixed Income-Like SEC Registered Funds and given the limited number of insurers investing in the funds on the NAIC Bond Fund List, the SVO proposed eliminating this list when the four funds come up for renewal in 2020 and migrating them over to the new NAIC Fixed Income-Like SEC Registered Funds list.

2. The Referral - The Task Force on the October 31st call requested a referral to the Working Group to consider and advise the Task Force on any issues or concerns it may have with adopting the amendment to: A) rename the “NAIC U.S. Direct Obligations/Full Faith and Credit Exempt Money Market Funds List” to the “NAIC U.S. Government Money Market Fund List” for cash equivalent reporting on Schedule E, Part 2; and B) eliminating the “NAIC Bond Fund List” that is referenced in *SSAP No. 26R – Bonds* in 2020 and migrating these funds over to the “NAIC Fixed Income-Like SEC Registered Funds List” that will be reported on Schedule D, Part 2 under *SSAP No. 30R – Unaffiliated Common Stock*.

Attached is the memorandum and draft amendments prepared by the staff for this request. Please direct any questions to Charles Therriault of the SVO.

G:\SECVAL\DATA\Vos-tf\Meetings\2020\Referrals outbound\SAPWG\Bond Fund and US Govt Fund\VOSTF 2019 - Bond and US Govt Fund Refer to SAPWG.docx



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 Rename the U.S. Direct Obligations/Full Faith and Credit Exempt List to the NAIC U.S. Government Money Market Fund List and Discontinue the NAIC Bond Fund List

DATE: September 30, 2019

1. Summary – The P&P Manual authorizes the SVO to maintain two special fund list. The first is the NAIC U.S. Direct Obligations/Full Faith and Credit Exempt Money Market Funds List. This list of Money Market Funds (MMF) gets special treatment because they can be reported as a cash equivalent on Schedule E, Part 2. The SVO proposes simplifying the title of this list to “NAIC U.S. Government Money Market Fund List.” This is only a title change to simplify the title of the list.

The second is the NAIC Bond Fund List, where the SVO reviews that a fund maintains the highest credit quality rating, maintains the highest market risk rating (this rating type that is no longer assigned), and invests 100% of its total assets in U.S. Government securities along with several other restrictive criteria. Only four funds qualify for this list and the four insurers invested in the fund have a combined exposure of \$11.8 million BACV in one of the four qualify funds as of December 31, 2018. With the adoption of the Comprehensive Instructions for Fund Investments on April 7th that provided new instructions for Fixed Income-Like SEC Registered Funds and given the limited number of insurers investing in the funds on the NAIC Bond Fund List, the SVO proposes eliminating this list when the four funds come up for renewal in 2020. The funds on the NAIC Bond Fund List would be eligible for NAIC Fixed Income-Like SEC Registered Funds List and the SVO would be willing to allow these fund issuers to apply to be on this new list at their renewal, if they were so interested. This change would require a referral to the Statutory Accounting Principles (E) Working Group as the NAIC Bond Fund List is referenced in SSAP No. 26R – Bonds.

2. Proposed Amendment – The text referencing these instructions for U.S. Direct Obligations/Full Faith and Credit Exempt Money Market Funds List and NAIC Bond Fund List is shown below, edits in red-underline, as it will appear in the 2019 P&P Manual format.

| | | |
|--|------------------|------------------|
| EXECUTIVE OFFICE • 444 North Capitol Street NW, Suite 700 • Washington, DC 20001-1509 | p 202 471 3990 | f 816 460 7493 |
| CENTRAL OFFICE • 1100 Walnut Street, Suite 1500 • Kansas City, MO 64106-2197 | p 816 842 3600 | f 816 783 8175 |
| CAPITAL MARKETS & INVESTMENT ANALYSIS OFFICE • One New York Plaza, Suite 4210 • New York, NY 10004 | p 212 398 9000 | f 212 382 4207 |

www.naic.org

2019 P&P Manual

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

The NAIC U.S. Government Money Market Fund List U.S. Direct Obligations/Full Faith and Credit Exempt Money Market Funds List

247. **Regulatory Treatment of Eligible Funds** – A money market mutual fund on the [NAIC U.S. Government Money Market Fund List U.S. Direct Obligations/Full Faith and Credit Exempt List](#) is reported as a cash equivalent on Schedule E, Part 2 on the “Exempt Money Market Mutual Funds – as Identified by the SVO” line. These “exempt” money market mutual funds are reported at fair value and incur a zero percent (0%) risk-based-capital (RBC) charge. Other money market mutual funds are also reported as cash equivalents on Schedule E, Part 2 on the “All Other Money Market Mutual Funds” line. The “all other” money market mutual funds are also reported at fair value but incur an RBC charge similar to other cash equivalents.
248. **Required Documentation** – An insurance company or the sponsor of a money market mutual fund requests an SVO evaluation that a money market mutual fund is eligible to be listed on the [NAIC U.S. Government Money Market Fund List U.S. Direct Obligations/Full Faith and Credit Exempt List](#) by submitting the following documentation to the SVO:
- The money market mutual fund application form.
 - Authorization letter requesting review of the fund for the purpose of being added to the List.
 - The most recent fund:
 - Prospectus;
 - Statement of Additional Information (SAI); and
 - Annual, and if available, the semi-annual report.
 - Rating letter from an NAIC CRP dated in the year of the filing.
249. **Eligibility Criteria** – A money market mutual fund is eligible for inclusion on the [NAIC U.S. Government Money Market Fund List U.S. Direct Obligations/Full Faith and Credit Exempt List](#) if the fund meets the following conditions:
- The fund maintains a money market mutual fund rating of AAAm from Standard & Poor’s or Aaa-mf from Moody’s Investor Services or an equivalent money market mutual fund rating from any NAIC CRP.
 - The fund maintains a stable net asset value per share of \$1.00.
 - The fund allows a maximum of seven-day redemption of proceeds.
 - The fund invests 100% of its total assets in securities that are direct obligations of the U.S. Government and/or in securities that are backed by the full faith and credit of the U.S. Government or collateralized repurchase agreements comprised of such obligations at all times.
NOTE: Please refer to text below for a list of securities considered to be direct obligations of the U.S. Government and entities that are entitled to the full faith and credit of the U.S. Government.
250. **Verification Procedure** – Upon receipt of the documentation, the SVO examines the prospectus, schedule of fund portfolio holdings and related materials to verify that the fund meets the established criteria.

The NAIC Bond Mutual Fund List

~~251. **Regulatory Treatment of Eligible Funds**—A bond mutual fund on the NAIC Bond Mutual Fund List is in scope of SSAP No. 26R—Bonds, reported with an **NAIC 1** designation on Schedule D, Part 1—Long Term Bonds on the “SVO Identified Funds—Bond Mutual Funds” line. The insurance company reports an **NAIC 1** Designation in accordance with Annual Statement Instructions. These investments are reported at fair value unless the investment qualifies for and the reporting entity elects systematic value.~~

~~252. **Required Documentation**—An insurance company or the sponsor of a bond mutual fund requests an SVO evaluation that a bond mutual fund is eligible for inclusion on the Bond Mutual Fund List by submitting the following documentation to the SVO:~~

- ~~▪ The bond fund application form.~~
- ~~▪ Authorization letter requesting review of the fund for the purpose of inclusion on the Bond Mutual Fund List.~~
- ~~▪ The most recent fund:
 - ~~○ Prospectus;~~
 - ~~○ Statement of Additional Information (SAI); and~~
 - ~~○ Annual, and if available, the semi-annual report.~~~~
- ~~▪ Rating letter from an NAIC CRP dated in the year of the filing.~~

~~253. **Eligibility Criteria**—A bond mutual fund is eligible for inclusion on the Bond List if the fund meets the following conditions:~~

- ~~▪ The fund shall maintain the highest credit quality rating given by an NAIC CRP.~~
- ~~▪ The fund shall maintain at least the highest market risk rating given by an NAIC CRP to a fund that invests in class 1 bonds that are issued or guaranteed as to payment of principal and interest by agencies and instrumentalities of the U.S. Government, including loan backed bonds and collateralized mortgage obligations, and collateralized repurchase agreements comprised of those obligations.~~
- ~~▪ The fund shall allow a maximum of seven-day redemption of proceeds.~~
- ~~▪ The fund shall invest 100% of its total assets in the U.S. Government securities listed in the section below; class 1 bonds that are issued or guaranteed as to payment of principal and interest by agencies and instrumentalities of the U.S. Government, including loan backed bonds and collateralized mortgage obligations, and collateralized repurchase agreements comprised of those obligations at all times.~~
- ~~▪ The fund shall declare a dividend of its net investment income each day prior to calculating its net asset value per share.~~
- ~~▪ The fund shall not invest in any derivative instruments, as that term is defined in the NAIC *Accounting Practices and Procedures Manual*.~~
- ~~▪ The fund shall not invest in any bonds that receive some or all of the interest portion of the underlying collateral and little or no principal, or in any bonds with coupons which reset periodically based on an index and which vary inversely with changes in the index.~~
- ~~▪ The fund shall not invest in the following types of securities: (a) leveraged or deleveraged notes that pay a multiple or fraction of an index or indices; (b) notes that pay principal or interest linked to foreign currencies, non-U.S. dollar interest rates, equity or commodities indices or any other index that is not composed of U.S. dollar denominated fixed-income instruments; or (c) notes that pay principal or interest linked to more than one index.~~

~~254. **Verification Procedure**— Upon receipt of the documentation, the SVO examines the prospectus, schedule of fund portfolio holdings and related materials to verify that the fund meets the established criteria.~~

...

g:\secval\data\vos-tf\meetings\2019\october\oct.31\instructions for etf with preferred and bonds\2019-012-01 -task force 2019 amend pp to add instructions for etf with preferred and bonds.docx