

U.S. Treasury Securities Process

9. U.S. Treasury Securities are an Investment Security added to the U.S. Treasury Securities Process automatically by electronic processes administered by the SVO and assigned an **NAIC 1** Designation and an NAIC Designation Category of **NAIC 1.A** by a policy-based convention. Insurance companies shall not report Regulatory Transactions as U.S. Treasury Securities and the NAIC staff shall not add a Regulatory Transaction to the U.S. Treasury Securities Process.

Exempt U.S. Government Securities Process

10. Exempt U.S. Government Securities are an Investment Security reported by the insurance company to the NAIC, subsequently added by NAIC staff to the Exempt U.S. Government Securities Process and assigned **NAIC 1** Designation and an NAIC Designation Category of **NAIC 1.A** pursuant to a policy-based convention. Insurance companies shall not report Regulatory Transactions as exempt U.S. Government Securities, and the NAIC staff shall not add a Regulatory Transaction to the Exempt U.S. Government Securities Process.

Reference to SVO List of Investment Securities

11. **Acknowledgement** – The NAIC, acting by and through its VOS/TF and its Reinsurance (E) Task Force, acknowledges that the phrase “Securities Listed by the SVO,” used in Section 3 B. of the NAIC *Credit for Reinsurance Model Law* (#785) and Section 10 A. (2) of the NAIC *Credit for Reinsurance Model Regulation* (#786) refers to the SVO List of Investment Securities as defined above provided that for purposes of Model #785, the phrase Securities Listed by the SVO also includes:
 - All U.S. Treasury Securities whether or not on the U.S. Treasury Securities Process Sub-List of the SVO List of Investment Securities as owned by an insurance company.
 - Any is a U.S. Government Exempt security not owned by an insurance company and therefore not on the SVO Exempt U.S. Government Securities Process Sub-List of the SVO List of Investment Securities.
 - Such other or additional type or class of securities as the Reinsurance (E) Task Force shall from time to time determine are suitable for use as collateral in reinsurance transactions and are added to this definition by the VOS/TF at its request.

12. To avoid confusion, and for purposes of this acknowledgment, the Filing Exempt Securities Process included in the definition of SVO List of Investment Securities includes the SVO listed securities referred to as those “deemed exempt from filing” in the cited sections of the Model #785 and Model #786.

Status of an Investment on the SVO List of Investment Securities

13. The reference to “Securities Listed by the SVO,” used in Model #785 and Model #786, refers solely to the individual, stand-alone investment purchased by an insurer and filed with the SVO to obtain an NAIC Designation and to be added to the SVO List of Investment Securities published in the AVS+ product.
14. References to “Securities Listed by the SVO” as eligible collateral for the purposes of reinsurance arrangements specified in Model #785 and Model #786 reflect that the specific insurer owns the Investment Security and has a corresponding right to receive the cash flow represented by the Investment Security from the security’s issuer, which is the right an insurer may pledge as collateral.
15. An Investment Security on the SVO List of Investment Securities **cannot be assumed or presumed to constitute** “Primary Security” as defined in the phrase “SVO Listed” in *Actuarial Guideline XLVIII—Actuarial Opinion and Memorandum Requirements for the Reinsurance of Policies Required to be Valued Under Sections 6 and 7 of the NAIC Valuation of Life Insurance Policies Model Regulation* (AG 48) or in the NAIC *Term and Universal Life Insurance Reserve Financing Model Regulation* (#787).
16. Whether an Investment Security on the SVO List of Investment Securities qualifies as “Primary Security” as defined in the NAIC *Valuation of Life Insurance Policies Model Regulation* (#830) or Model #787 is not an issue within the scope of the charges entrusted to the VOS/TF or within the analytical function or role of the or SSG.
17. Whether a Regulatory Transaction as defined in this Manual has any status under Model #785, Model #786, Model #830 or Model #787 is not an issue within the scope of the charges entrusted to the VOS/TF or within the analytical function or role of the SVO or SSG.

PRODUCTION OF 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 5.B GI 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 5.B GI are not met.
29. Securities with NAIC 5.B GI Designation Categories are deemed to possess the credit characteristics of securities assigned an NAIC 5.B Designation Category. A security assigned an NAIC 5.B GI Designation Category incurs the regulatory treatment associated with an NAIC 5.B Designation Category.
30. Securities an insurance company previously assigned as NAIC 5.B GI are permitted to subsequently receive this NAIC Designation Category if the requirements for an NAIC 5.B GI Designation Category 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 5.B GI Designation Category 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.B refers to General Interrogatory and distinguishes NAIC 5.B GI from an NAIC 5.B Designation Category. 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.

SVO NOTCHING GUIDELINES

Definition and Purpose

40. Notching is defined as the process used to make distinctions between different liabilities in an issuer capital structure to reflect differences in credit or other non-payment risk smaller than a whole grade. Notching expresses differences in expected loss (i.e., severity) of an issuer's liabilities by their relative priority of claim in bankruptcy.
41. With the exception of **NAIC 6**, notching distinctions are expressed by combining an NAIC Designation with an NAIC Designation Modifier to produce an NAIC Designation Category. For example, as shown in the table above, **NAIC 1** is combined with NAIC Designation Modifier 1.A to produce the NAIC Designation Category 1.A. Modifiers are used with or assigned to the **NAIC 6** Designation.

Notching NAIC Designation Categories (to Reflect Credit Risk)

42. **Illustration** – The distinctions in credit risk made in the notching process involve (conceptually) the issuer's actual capital structure. The hypothetical capital structure below is shown to illustrate and explain notching:

Senior secured	Notch up from the benchmark
Senior unsecured	Benchmark NAIC Designation
Senior subordinated	Notch down from the benchmark
Junior subordinated	Notch down from benchmark
Preferred stock	Notch down from benchmark

Methodology

43. The SVO determines the benchmark NAIC Designation Category for the senior unsecured obligation of the issuer or its equivalent. The SVO adjusts the benchmark NAIC Designation Category up or down to reflect the difference in risk between the benchmark security and the specific liability under review by the SVO.

SVO Guidelines for Notching

44. The SVO shall notch an NAIC Designation Category for an issuer up or down to reflect the position of a specific liability in the issuer's capital structure.

45. Notching upward from a benchmark NAIC Designation Category is almost exclusively associated with transactions in which the SVO determines that collateral act to further reduce the probability of default from that implied by the issuer's senior unsecured NAIC Designation Category.
46. In determining the number of notches that should be applied to a security, the SVO shall apply the following guidelines.

Notching Investment Grade Issuers

47. Notching for issuer's whose senior unsecured benchmark NAIC Designation is **NAIC 1** and **NAIC 2** is therefore based on the following general guidelines:
- **Secured debt** may be designated one notch above the senior unsecured issuer designation.
 - **Subordinated debt** (including junior and senior subordinated) are generally designated one notch below the senior unsecured rating.
 - **Preferred debt** will generally be designated one notch below subordinated debt (two below senior unsecured or senior implied).
 - **Holding company debt** is generally designated at or below the lowest rated debt security that would be assigned at the principal operating company.

Notching for Non-Investment Grade Issuers

48. Given the risks associated with non-investment grade issues, notching for issuer's whose senior unsecured benchmark NAIC Designation is **NAIC 3**, **NAIC 4** and **NAIC 5** requires grater professional judgment and discretion.
49. As such, notching differentials for issuers with **NAIC 3**, **NAIC 4** and **NAIC 5** Designations may be wider than for issuer's whose senior unsecured NAIC Designation is **NAIC 1** or **NAIC 2**.

Notching for NAIC Designation Subscript (to Reflect Non-Payment Risk Unrelated to Credit Risk)

50. **Grant of Significant Discretion** – The SVO is granted significant discretion to determine the number of notches it will assign to a security to reflect other non-payment risk. This discretion is to be exercised in the context of the regulatory objective and purpose of this procedure. SVO determinations made under this subparagraph are subject to review in accordance with the procedures described of this Part, above.

Relevant Considerations

51. The name given to the security is not relevant to a determination whether this subparagraph should be applied. The relevant criterion is whether the risks in the security are clearly credit risks or whether they are not clearly credit risks.
52. Factors the SVO may deem relevant to the question of notching for other non-payment risk may include:
 - Any security or financial instrument denominated with a term associated with fixed income investments must contain a clearly stated obligation to pay a return and to repay the amount of the principal repayment. Otherwise it is not rational or possible to assign an NAIC Designation.
 - Any security or financial instrument denominated as fixed income that does not contain a legally binding obligation to pay shall not be assigned an NAIC Designation and instead will be reported to the VOS/TF and the Chief Examiner of the State of Domicile.
 - Any security or financial instrument that is denominated as fixed income and that contains a promise to pay that is otherwise conditional may be notched either under this subparagraph to reflect other non-payment risks or under the notching procedure for credit risk to reflect the expected loss of that obligation in the issuer's specific capital structure, depending on which approach seems more appropriate to the SVO.
53. The widest degree of notching for a security or financial instrument is likely to be for a security that is denominated as fixed income, but which is deemed to be a perpetual investment and to not require payment of dividends.
54. In contracts that permit the issuer flexibility to not make payments, the SVO would focus on the degree of financial discretion afforded the issuer to not make payments and the circumstances under which that financial flexibility will be exercised.
55. In contracts where the insurer agrees to accept a risk or participate in an activity that may reduce either the interest or dividend otherwise agreed on or the amount to be repaid to less than the original principal investment, the SVO would consider whether the risk of a loss is structurally or otherwise mitigated.
56. Notching differentials are expected to be wider for **NAIC 3**, **NAIC 4** and **NAIC 5** issuers because the issuer's credit risk is deemed to increase the likelihood that the issuer will avail itself of contractually provided flexibility to not pay or increase the likelihood of a loss as a result of the insurer's participatory activity.

57. Deferral of dividends in a security denominated preferred stock is presumed to be subject to notching for credit risk subject to an SVO determination that the denomination is not truly reflective of the terms of the agreement in which case it may be more appropriately notched for other than credit risk.
58. In a given capital structure, the priority of payment due to an investor may be so subordinated as to require treatment under these guidelines for other non-payment risk. This is especially true where deep subordination is combined with a right to defer interest.

SVO RESPONSIBILITY FOR INVESTMENT RISK ANALYSIS OF NEW FINANCIAL PRODUCTS

59. The SVO has responsibility for assisting NAIC members and individual states to assess investment risk in new securities and financial products. The SVO exercises this responsibility:

- When requested to do by the VOS/TF, any of its working groups, any other NAIC task force or working group or any individual state insurance department.
- Through the RTAS – Emerging Investment Vehicle Service process.
- Through ongoing research and analysis activity aimed at identifying both broad developments in the capital markets and the introduction of specific new classes of securities that insurance companies may purchase.
- By providing biannual or more frequent reports to the VOS/TF on innovative structures filed by insurance companies and the risks they contain.
- By sharing information obtained through interaction with market participants with the VOS/TF.

REPLICATION (SYNTHETIC ASSET) TRANSACTIONS

NOTE: See “Specific Populations of Securities Not Eligible for Filing Exemption” in “Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities” in Part Three.

Definitions

60. The following terms shall have the meaning ascribed in this section. The definitions of derivative instruments set forth in *SSAP No. 86—Derivatives* are incorporated by reference.

APPROVED RSATs

Safe Harbor – Defined RSATs

61. Any transaction that meets either of the following conditions:

- Any transaction structured according to the following defined transaction types shall be presumed to be an Approved RSAT and should be submitted to the SVO pursuant to this paragraph. Transactions that are structured to contain elements of risk other than those normally associated with the Defined RSAT descriptions below, and transactions involving assets that would not normally qualify for an NAIC Designation, are not eligible for safe harbor treatment and must be submitted to the SVO pursuant to the paragraph titled “Transactions Subject to RSAT Approval Review” below. If the SVO receives a transaction that does not qualify for an NAIC Designation but would otherwise qualify as an Approved RSAT, the SVO will bring the transaction to the attention of the VOS/TF and await instructions on how to proceed with it.
 - *Bond with Interest Rate Swap* – In this RSAT, the insurer enters into a swap agreement to exchange a floating interest rate for a fixed interest rate, or vice versa.
 - *Bond with Credit Default Risk Swap* – In this RSAT, the insurer enters into a credit default swap to exchange the credit default risk of a bond for that of another bond.
 - *Bond with Total Return Swap* – In this RSAT, the insurer enters into a total return swap to exchange the return of one Basket or Index of bonds for the return of another Basket or Index of bonds.
 - *Bond with Foreign Currency Swap* – In this RSAT, the insurer enters into a currency swap to exchange the right to receive principal and/or interest in the currency of one country for that of another. A foreign currency swap can be structured on a fixed or floating rate bond. The swap can involve any currency.

- *Bond with Equity Option* – In this RSAT, the insurer holds a bond and enters into a call option to purchase common stock or a call on an equity index
- *Convertible Bond with Sale of Equity Option* – In this RSAT, the insurer holds a convertible bond and enters into an agreement to sell the equity conversion rights connected with the bond to another party.
- *Bond with Index Amortizing Interest Rate Swap* – In this RSAT, the insurer enters into an agreement to exchange fixed interest rate payments for floating interest rate payments or vice versa. The notional amount of the swap, and therefore the size of the interest rate swap, amortizes by reference to an index, usually also tied to interest rates.
- *Bond with Interest Rate Swap and Swaption Agreement* – In this RSAT, the insurer enters into two agreements. The first agreement is to exchange a fixed interest rate for a floating interest rate or vice versa. In the second agreement, the insurer enters into a swaption agreement by which it allows itself the option of transferring its obligations under the swap agreement.
- *Bond with Interest Rate Swap and Interest Rate Cap/Floor* – In this RSAT, the insurer enters into two agreements. The first agreement is to exchange a fixed interest rate for a floating interest rate or vice versa. In the second agreement, the insurer limits its exposure above or below a certain interest rate level by entering into a cap or floor agreement.

TRANSACTIONS SUBJECT TO RSAT APPROVAL REVIEW

62. Transactions that are not structured according to one of the transaction types defined above must be submitted to the SVO for a determination of whether or not the transaction is an Approved RSAT. This determination shall be made through a review of the submitted documents that describe the characteristics of the derivative and cash components of the transaction. The description submitted shall include the following:
- An identification of the cash flows in the transaction; both from the insurer to other parties and from other parties to the insurer.
 - An identification of the resulting synthetic
 - A demonstration of how the cash flows serve to produce the synthetic asset.

63. The documentation should demonstrate that the combined cash flows will achieve the economic performance sought to be produced by the insurer and, therefore, qualify the transaction as an Approved RSAT. If the SVO receives a transaction that does not qualify for an NAIC Designation but would otherwise qualify as an Approved RSAT, the SVO will bring the transaction to the attention of the VOS/TF and await instructions on how to proceed with it.

- **Basket** – A composite of specific financial instruments that are determined by agreement between two parties to be used as a statistical benchmark.
- **Cash Component** – The instrument, or portfolio of instruments, owned by the insurance company that is identified by the insurer as the cash instrument component of the RSAT. In an RSAT, the credit quality of the Cash Component may differ from the credit quality of the reference securities.
- **Change in Credit Profile** – An RSAT where the credit risk denoted by NAIC Designation and/or NAIC CRP rating, of the Cash Component is different from the credit risk of the replicated (synthetic) asset. Examples of transactions that constitute a change in credit profile may include:
 - *A Bond with Credit Default Risk Swap* – Where the risk of loss of principal results from the potential of default by an obligor different from the Cash Component obligor. This RSAT can also be structured to use the same obligor for the Cash Component and the replicated (synthetic) asset, but where the replicated (synthetic) asset is in a different position in the capital structure of the obligor. For example, the swap may result in a change from senior creditor's status to one of a subordinated debt holder.
 - *A Bond with Total Return Swap* – Where the obligors in the Cash Component portfolio are different from those in the derivative instrument component. Examples of transactions that do not, on their own, constitute a change in credit profile include:
 - A Bond with Interest Rate Swap.
 - A Bond with Foreign Currency Swap.
- **Effective RSAT** – A reported transaction that meets the following conditions:
 - The transaction is determined to be an Approved RSAT.
 - The Replicated (Synthetic) Asset is an otherwise permissible investment.
 - At the time the RSAT is entered into, the insurer's investment in the cash and derivative components have a market value that is not materially different from the market value ascribed to the RSAT.

- The insurer's maximum potential loss in the Replicated (Synthetic) Asset does not exceed the sum of the book/adjusted carrying value of the Cash Component, and the derivative component.
- The RSAT consists of a fixed income Cash Component and a derivative component and the term of the derivative component does not exceed the term to maturity of the Cash Component.
- At no time is there exposure to a derivative transaction without a corresponding Cash Component assigned exclusively to the Replicated (Synthetic) Asset.
- **Identical RSAT** – An RSAT entered into by multiple, yet legally separate and distinct, insurance companies of the same insurance company group through separate derivative contracts, but utilizing the same type of derivative transaction, Cash Component, counterparty, transaction effective date, scheduled termination date and assigned a single CUSIP Identifier.
- **Index** – A composite of financial instruments whose composition is determined by application of objective, pre-defined rules to be used as a statistical benchmark. Financial instruments may be added to or deleted from the index universe.
- **Reference Security** – A financial instrument or instruments whose creditworthiness is referenced in a derivative agreement (typically, a credit default risk swap) and that serves as the instrument by which a credit event is determined or triggered.
- **Replication (Synthetic Asset) Transaction (RSAT)** – A derivative transaction entered into in conjunction with other investments in order to reproduce the investment characteristics of otherwise permissible investments. Notwithstanding the exemption of short-term investments from filing with the SVO, the term RSAT includes long-term transactions (i.e., those with a when-issued maturity of a year or more) and short-term transactions (i.e., those with a when issued maturity of a year or less). Although transactions structured with a futures or forward equity contract may not exactly reproduce a specific asset, these transactions are permitted to the extent such RSATs are permissible investments according to the insurer's state of domicile. A derivative transaction entered into by an insurer as a hedging or income generation transaction shall not be considered to be a replication (synthetic asset) transaction. The insurer shall be responsible for determining that a derivative transaction is considered to be either a hedging, income generation or replication (synthetic asset) transaction prior to filing the transaction with the SVO.

NOTE: See *SSAP No. 86—Derivatives* for a definition of hedging and income generation.

- **RSAT Form** – The Replication (Synthetic Asset) Transaction Form used to report RSATs.
- **RSAT-CCA Form** – The Replication (Synthetic Asset) Transaction – Credit Change Annex Form used to report transactions where the RSAT results in a Change in Credit Profile from that of the Cash Component.
- **RSAT Basket Form** – The Replication (Synthetic Asset) Transaction Form used to Report RSATs using Baskets.
- **RSAT Fixed Income Index Form** – The Replication (Synthetic Asset) Transaction Form used to report RSATs using Indices discussed and defined in this Section.
- **RSAT Index List Application** – The Replication (Synthetic Asset) Transaction Form used to apply for inclusion on the NAIC Approved RSAT Index List.

Instruction to Report Replication (Synthetic Asset) Transactions

64. **Instruction** – Insurance companies shall report all RSAT transactions, including RSAT transactions of duration less than 365 days, to the SVO and the SVO shall apply the instructions in this section to all reported RSATs including Baskets and Indices.
65. **Special Instruction Regarding Identical RSATs** – Only one insurance company that is a member of an insurance company group that has engaged in an Identical RSAT is required to file the RSAT with the SVO. All of the rules and procedures specified in this section shall be applicable to that filing.
66. Notwithstanding this special instruction, all of the members of the insurance company group that have entered into an Identical RSAT shall nevertheless fully report their holdings as required by annual statement instructions for Schedule DB, Part C.
67. Any state insurance regulator who questions whether the RSAT entered into by members of an insurance company group meets the definition of an Identical RSAT may require the members of the group to file relevant information with the SVO so that the SVO may verify whether transactions claimed to be identical are identical within the meaning of the definition and/or whether the insurance companies have otherwise appropriately reported the RSAT transaction.

68. The SVO shall have authority to make inquiries of insurance companies and to request insurance companies to file relevant information with it so it may verify whether transactions claimed to be identical are identical within the meaning of the definition and/or whether the insurance companies have otherwise appropriately reported the RSAT transaction.
69. **Counterparty Risk-Based Capital** – The NAIC Designation assigned to a RSAT does not capture any counterparty risk associated with any derivative component of the RSAT. The credit risk of any particular counterparty is captured in the risk-based capital charge of the counterparty reported in Schedule DB, Part D, Section 1.

INITIAL REPORTING OF REPLICATION (SYNTHETIC ASSET) TRANSACTIONS

Informational Requirements – General

70. Each reporting insurance company is required to file the information listed below for every RSAT filing. Additionally, for those RSATs exhibiting a Change in Credit Profile, the reporting insurance company shall be required to file the information listed under the paragraph titled “Additional Instructions for RSATs with a Change in Credit Profile” below.
71. General Filing Instructions:
- RSAT Form.
 - If any Cash Component is required to be filed with the SVO and is not on the VOS Process with a current year Designation, the reporting insurance company is required to follow the reporting conventions and file the required documents.
 - The reporting insurance company is required to file the prospectus, offering circular, detailed term sheet, trade confirmation, swap agreement, call option agreement, foreign currency agreement or other agreement or document, as appropriate to the transaction, corresponding to each derivative component of the reported Approved RSAT.
 - If the derivative component of the Approved RSAT relies on a counterparty that is not on the List of Counterparties Designated by the SVO refer to that section for a description of analytical procedures and informational requirements.
72. Additional Instructions for RSATs with a Change in Credit Profile:
- RSAT-CCA Form.

- If the transaction is one that involves securities, including Reference Securities that require an NAIC Designation, the reporting insurance company is required to follow the reporting conventions and file the required documents for such securities.

Procedures Applied to Initial Reports of Replication (Synthetic Asset) Transactions

73. **Effective RSAT** – The SVO shall verify that the reported RSAT meets those standards of effectiveness set forth in this section. The reporting insurance company shall have responsibility for ensuring that the standards of effectiveness set forth in section titled Effective RSAT have been met.
74. **Credit Assessment** – The SVO shall apply the procedures listed under the paragraph titled “General Procedures” below for every filing. Additionally, for those RSATs exhibiting a Change in Credit Profile, the SVO shall apply the procedures set forth in the paragraph titled “Additional Procedures for RSATs with a Change in Credit Profile” below.
75. **General Procedures:**
- If the Cash Component is of a type that is required to be filed with the SVO and is not on the VOS Process with a current year designation, the SVO shall apply the methodologies set forth in this Manual.
 - If any counterparty involved in the RSAT is not currently listed on the SVO’s List of Counterparties Designated by the SVO, the SVO shall apply the procedures set forth in this Manual.
 - The SVO shall review the documents corresponding to each derivative component of the reported Approved RSAT to verify that the relationships and identities of the parties to the agreement(s) are as reported on the RSAT Form.
 - If the SVO determines that the documentation provided comports with the reported RSAT, then the analyst shall assign the NAIC Designation of the Cash Component to the RSAT.
76. **Additional Procedures for RSATs with a Change in Credit Profile** – If the transaction involves securities, including Reference Securities, which are on the VOS Process with a current year designation, the SVO shall assign that Designation associated with the Reference Securities to the RSAT.

- If the transaction involves securities, including Reference Securities that are not on the VOS Process with a current year designation, the SVO shall apply the methodologies in this Manual to the securities. Upon determination of an NAIC Designation for such securities, the SVO shall apply that Designation associated with the Reference Securities to the RSAT.

SUBSEQUENT REPORTING OF REPLICATION (SYNTHETIC ASSET) TRANSACTIONS

Informational Requirements – General

77. Each reporting insurance company is required to file the information listed below for every RSAT filing. Additionally, for those RSATs exhibiting a Change in Credit Profile, the reporting insurance company shall be required to file the information listed under the paragraph titled “Additional Instructions for RSATs with a Change in Credit Profile” below.
78. General Filing Instructions:
- For the Cash Component, file the required documentation.
 - There are no additional subsequent reporting requirements if there are no changes in any of the components of the RSAT. Any sale, termination or modification of the component pieces of an Approved RSAT must be reported to the SVO within 30 days. This can be done by submitting to the SVO either a Material Change ATF Form or a Renumbering Request for the affected RSAT. Any such sale, termination or modification that results in the RSAT ceasing to be effective pursuant to the section titled “Effective RSAT” will immediately terminate the replication (synthetic asset) transaction.
79. **Additional Instructions for RSATs with a Change in Credit Profile** – File the required documentation required by this Manual for securities, including Reference Securities, on the VOS Process. If a security is no longer listed on the VOS Process, file the documentation required by this Manual.

Procedures Applied to Subsequent Reports of Replication (Synthetic Asset) Transactions

80. **Credit Assessment** – The SVO shall apply the procedures listed below for every filing. Additionally, for those RSATs exhibiting a Change in Credit Profile, the SVO shall apply the procedures set forth in the paragraph titled “Additional Instructions for RSATs with a Change in Credit Profile” below.
81. General Procedure:
- The SVO shall monitor the NAIC Designation assigned to the Cash Component.

- The SVO shall monitor the NAIC Designation assigned to the counterparties to the derivative component of the RSAT.
- The reporting insurance company must report a change in the documentation relating to any derivative component to the SVO. The SVO shall assess the significance of such change.

82. **Additional Procedures for RSATs with a Change in Credit Profile** – The SVO shall monitor the NAIC Designation assigned to any security, including Reference Securities, involved in the RSAT.

ADDITIONAL PROCEDURES FOR RSATs USING BASKETS
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Initial Reporting

83. **Informational Requirements** – Reporting insurance companies are required to file the information listed below for each replication they enter into using a Basket:

- RSAT Basket Form.
- If any of the component instruments in a Basket are not on the VOS Process with a current year Designation, the reporting insurance company is required to follow the reporting conventions and file the required documents set forth in this Manual.
- If the derivative component of the RSAT relies on a counterparty that is not on the List of Counterparties Designated by the SVO the informational requirements identified above apply.

Procedures Applied to Initial Reports of Baskets

84. **Effectiveness Testing** – The SVO shall verify that the reported RSAT meets those standards of effectiveness set forth in the section titled Effective RSAT. The reporting insurance company shall have responsibility for ensuring that the standards of effectiveness set forth in the section titled Effective RSAT above have been met.
85. **Credit Assessment** – If any component instrument of a Basket is not on the VOS Process with a current year Designation, the SVO shall apply the methodologies in Part Three of this Manual.
86. **Counterparty** – If any counterparty named in the RSAT is not currently listed on the SVO's List of Counterparties Designated by the SVO, the SVO shall the corresponding procedures in this Manual.

Subsequent Reporting

87. **Informational Requirements** – Reporting insurance companies are required to file the information listed below for each replication they enter into using a Basket on an annual basis.

- If there are additions or deletions to the component instruments in a Basket, the SVO should be notified within 30 days. If any new component instrument in a basket is not on the VOS Process, the reporting insurance company is required to follow the reporting conventions and file the required documents for each of those instruments.
- If any of the existing or new component instruments in a Basket are on the VOS Process, but do not have a current year Designation, the reporting insurance company is required to follow the reporting conventions and file the required documents for each of those instruments.

88. Procedures Applied to Subsequent Reports of Baskets:

- The SVO shall monitor the NAIC Designation of those Basket components with NAIC Designations.
- The SVO shall monitor the NAIC Designation assigned to the counterparty to the derivative component of the RSAT.

ADDITIONAL PROCEDURES FOR RSATs USING INDICES
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Initial Reporting

89. **Informational Requirements** – Reporting insurance companies are required to file an RSAT Fixed Income Index Form with the SVO for each replication they enter into using an equity or fixed income Index. An insurance company may only enter into an RSAT using a fixed income Index if the Index is listed on the SVO's RSAT Index List. Equity Indices are not required to be on the SVO's RSAT Index List as no credit quality evaluation is performed on equity investments.

90. Procedures Applied to Initial Reports of Indices:

- **Effectiveness Testing** – The SVO shall verify that the reported RSAT meets those standards of effectiveness set forth in the section titled Effective RSAT. The reporting insurance company shall have responsibility for ensuring that the standards of effectiveness set forth in the section titled Effective RSAT have been met.

- **Counterparty** – If any counterparty named in the RSAT Form is not currently listed on the SVO’s List of Counterparties Designated by the SVO, the SVO shall apply the corresponding procedures.
- **Verification** – The SVO will verify that any fixed income Index named in the RSAT Form is on the SVO’s current RSAT Index List.

Subsequent Reporting

91. Informational Requirements:

- Reporting insurance companies are not required to file any annual information with the SVO for RSATs using an Index as long as the Index, if it is a fixed income Index, remains on the SVO’s RSAT Index List. If a fixed Income index is removed from the list, any RSAT utilizing such Index will no longer qualify as an Approved RSAT.
- The SVO shall monitor the NAIC Designation assigned to the counterparty to the derivative component of the RSAT.

Procedures for Compilation of the RSAT Index List

92. **Compilation of List** – The staff is instructed to compile and maintain a list of fixed income indices that meet the standards identified in the RSAT Index List. The RSAT Index List may be used by reporting insurance companies when filing fixed income Index RSATs with the SVO. If the SVO determines that an Index does not meet the eligibility requirements set forth below, the Index will not be included on the list. Publication of an Index on the RSAT Index List does not imply an opinion of the quality of such Index or of the Index vendor.

93. **Eligibility Requirements** – A fixed income Index may be eligible for listing on the RSAT Index List if the Index meets the following requirements:

- **Rule-Based** – The Index is composed and valued based on the application of objective, pre-defined criteria. Additions to or deletions from the list must be made based on the application of such criteria.
- **Information Available** – Rating information about the components is, or can be made available, to the SVO.

- **Components Rated** – All, or substantially all, of the Index components are rated, or have obligors that are rated, by an NAIC CRP or have received a current year NAIC Designation from the SVO. In the event that not all of the Index components are NAIC CRP-rated or have a current year NAIC Designation, the reporting insurance company may either: (a) file the component with the SVO to obtain a Designation; or (b) assign an **NAIC 5*** Designation to the unrated instrument, as long as it is current on principal and interest or an **NAIC 6*** Designation if it is not or if the status is not determinable. Instruments assigned an **NAIC 5*** Designation or **NAIC 6*** Designation, on a combined basis, can represent no more than 5% of the Index’s total value.
- **Independent** – The Index is predominantly composed of instruments whose issuers are unaffiliated with the Index vendor.

94. **Initial Reporting** – In order to apply for listing of a fixed income Index on the RSAT Index List, a reporting insurance company should submit the following to the SVO:

- A listing of all Index components.
- The ratings of all NAIC CRP-rated Index components from all NAIC CRPs that have rated the component.
- The actual NAIC Designation for each Index component with an NAIC Designation or an equivalent NAIC Designation for each component rated by an NAIC CRP using the conversion instructions and the rating equivalents, if rated and monitored by one NAIC CRP, the equivalent NAIC Designation; if rated and monitored by two NAIC CRPs, then the lowest rating and if rated and monitored by three or more NAIC CRPs, then the second lowest rating. In the case of a security rated and monitored by three or more NAIC CRPs, the NAIC CRP ratings for a security are ordered according to their NAIC Designation equivalents and the rating that is second lowest will be selected, even if that rating is equal to that of the first lowest.
- A demonstration and certification by the insurance company, as evidenced by an executed certificate by an officer of the insurance company, that the eligibility requirements set forth in the “Eligibility Requirements” paragraph in the “Procedures for Compilation of the RSAT Index List” section above have been met.

95. **Subsequent Reporting** – The reporting insurance company shall annually submit to the SVO the items listed in the “Initial Reporting” paragraph of the “Procedures for Compilation of the RSAT Index List” section above for each fixed income Index it desires to maintain on the RSAT Index List. Any Index on the RSAT Index List for which the required documents are not submitted, or any Index that no longer meets the eligibility requirements set forth in section above, shall be deleted from the RSAT Index List.

THE REGULATORY TREATMENT ANALYSIS SERVICE – EMERGING INVESTMENT VEHICLE

Finding

96. The VOS/TF finds that the pace of financial innovation and extent of financial engineering requires close cooperation between regulated insurance companies, investment banks and other financial market participants and the regulators who must assess the solvency implications of financial innovation and engineering. This section establishes the mechanism for an insurance company or another market participant (Applicant) to apply to the SVO for the purpose of determining the probable regulatory treatment to be accorded to an Emerging Investment Vehicle (EIV) before it is sold to an insurance company, or for any other security.

Definition of Probable Regulatory Treatment

97. For purposes of this section, probable regulatory treatment means the professional opinion of the SVO as to the credit quality designation; and/or asset classification for statutory reporting purposes; and/or the valuation that would be accorded to the EIV under this Manual if it were purchased by an insurance company and reported to the SVO.
98. Probable regulatory treatment includes a statement by the SVO that, in its opinion:
- The existing regulatory framework already captures the risks posed by the security either through the mechanism of credit ratings, valuation policy or classification methodology;
 - The existing regulatory framework does not capture the risks posed by the security and that it is necessary to apply to the VOS/TF to develop an appropriate regulatory accommodation for the instrument; or
 - The SVO lacks an approved methodology that could be used to assess the risks contained in the EIV and that it is necessary to apply to the VOS/TF to develop an appropriate methodology.

Definition of EIV

99. For purposes of this section, an EIV is an investment security or other financial product that is newly offered and that contains characteristics or features not previously reviewed by the VOS/TF or the SVO for a determination of the probable regulatory treatment to be accorded to the EIV. An EIV may be “newly offered” in the sense that the security or financial product has not previously been known (and hence none of its characteristics or features are known) or in the sense that a security or financial product whose primary characteristics or features are understood has evolved to incorporate substantially different features or to contain significant innovation such that it should be considered as never having been reviewed by the VOS/TF or the SVO.

Who May Request an Analysis Under This Section

100. An EIV may be filed by:
- An insurance company or by another market participant (without the requirement of insurance company sponsorship); or
 - A state insurance regulator for any security owned by an insurance company under the authority and for purposes discussed in this Manual, subject only to the conditions imposed in this section and in other referenced sections.
101. The SVO is not authorized to require anyone to file a transaction as an EIV. However, nothing in this section limits the obligation or the authority of the SVO to report to the VOS/TF any transaction, whether or not filed with the SVO, that presents issues or contains features that require guidance from the VOS/TF.

Submission Procedure

102. To request an analysis of probable regulatory treatment of an EIV, the Applicant submits an original completed Application for Regulatory Treatment Analysis Service (Application) to the Director, SVO (the “Director”) or the Director’s designated representative. An Application shall be accompanied by written and substantially finalized documentation showing all material terms with the same specificity and clarity as the SVO requires to complete a purchased transaction. A copy of the prospectus or private placement memorandum will not be required if it is unavailable at the time of the filing of the Application, however, it may be required before a determination on the EIV in question can be made by the SVO.

Requirement of a Substantially Finalized Transaction

103. Analysis of probable regulatory treatment will be provided only for securities and financial products that have been substantially finalized in all material respects. The SVO is not authorized to assist the Applicant to structure a transaction to attain specific regulatory objectives. The SVO shall have full discretion to determine that the terms of a security or financial product as reflected in the documentation submitted with the Application indicate that the security or financial product is not substantially finalized.

Discretion

104. The Director shall have full discretion to reject an Application if, in the Director's sole discretion, acceptance of the Application would not meet the objectives of the NAIC Financial Condition Framework. The Director will communicate any such rejection to the Applicant and will return the Application fee and may communicate such rejection to the VOS/TF for informational purposes.

Communication of Determination

105. At the conclusion of the processing of the EIV, the SVO will provide a letter to the EIV Applicant setting forth its conclusions with respect to the issue(s) raised by the EIV.
106. If the SVO concludes that this Manual does not provide sufficient guidance to determine an NAIC Designation, valuation or classification for the EIV, or that in its opinion the NAIC Financial Conditions Framework does not clearly specify standards or criteria for responding to the issue(s) raised by the Applicant, it will so inform the Applicant and the VOS/TF.
107. Information provided as part of the RTAS – Emerging Investment Vehicle Application shall be treated as confidential by the SVO. The Applicant may communicate the content of the letter to anyone provided the Applicant also communicates that the purpose of the analysis reflected in the letter is regulatory. The Applicant may also provide copies of the SVO letter to anyone provided a complete copy of the SVO letter must be given.
108. If, after the SVO has communicated its decision to the Applicant, an insurance company purchases the EIV and reports it to the SVO, either on its own initiative or at the direction of an insurance regulator, the SVO may be required to enter its determination into NAIC systems, including systems accessible to the market participants for regulatory purposes. This shall not be considered a breach of the agreement to hold our determination confidential.

109. The regulatory expectation is that Applicants who advise insurance companies will make full disclosure of the SVO determination to any insurance company that requests such information, even if the conclusion is contrary to the Applicant's initial expectations.

Standing of EIV Application in the NAIC Financial Condition Framework

110. The activity authorized by this section is intended solely to facilitate the business and regulatory objectives of the NAIC and the financial solvency function of the VOS/TF. The SVO's acceptance of an Application does not convey any regulatory status or recognition to the EIV.
111. A preliminary NAIC Designation assigned under the procedure specified in this section is only valid for the day issued as such designation reflects the preliminary draft of documents and other information that have been presented to the SVO.
112. A preliminary NAIC Designation will not be published in the Database or the AVS+ Products and, therefore, cannot be used to report the credit quality of the security to the NAIC or any state insurance department. Only NAIC Designations published in the AVS+ Products may be used to report an investment to an NAIC member's state insurance department.
113. If an insurance company subsequently purchases the security, the purchasing company must file an Initial Report or, if the security is filing exempt, report the security in accordance with that procedure. The SVO shall apply its usual procedure for initially reported securities before assigning an NAIC Designation and publishing such NAIC Designation in the AVS+ Products.

LIST OF QUALIFIED U.S. FINANCIAL INSTITUTIONS

Regulatory Purpose and Objectives

114. The List of Qualified U.S. Financial Institutions established in this Part Two implements Section 3 C. (1) and Section 4 A. of the NAIC *Credit for Reinsurance Model Law* (#785) (Model Law).
115. Section 3 C. (1) of the Model Law permits an asset or a reduction from liability for reinsurance ceded by a domestic insurer to an assuming insurer. The asset or reduction may be in an amount held by or on behalf of the ceding insurer, including security in the form of a LOC issued or confirmed by a qualified U.S. financial institution. Section 4A of the Model Law defines the term “qualified U.S. financial institution,” which is hereby incorporated by reference.
116. The List of Qualified U.S. Financial Institutions is a compilation of the names of banks and nondepository lenders (financial institutions) that have applied to the NAIC to be identified as issuers of LOCs in support of reinsurance arrangements under the Model Law or state law provisions based on the Model Law.
117. The placement of the name of a financial institution on the List of Qualified U.S. Financial Institutions indicates that the SVO has verified that the applicant meets the financial and other eligibility standards specified in this part and that the financial institution has agreed to provide the SVO with any information necessary to permit the SVO to evaluate whether the financial institution continued to meet the eligibility standards specified in this Part.
118. The List of Qualified U.S. Financial Institutions is maintained for the use of state insurance regulators administering credit for reinsurance provisions in state law based on the Model Law and may also be used by insurance companies to identify financial institutions willing to support reinsurance arrangements as identified in Section 3 C. (1) and Section 4A of the Model Law.
119. The List of Qualified U.S. Financial Institutions implemented under this Part is not intended to be used for any other purpose or by any other person or entities. The placement of the name of a financial institution on the List of Qualified U.S. Financial Institutions is not an opinion as to any aspect of the financial institution’s operations, the appropriateness of doing business with the financial institution or the suitability or unsuitability of any financial institution on the list to serve as a provider of credit enhancement for securities transactions.

Directive to Compile the List of Qualified U.S. Financial Institutions

120. The SVO shall compile the List of Qualified U.S. Financial Institutions in accordance with the procedures and instructions provided in this section.

LIST OF NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATIONS

Establish a List of Nationally Recognized Statistical Rating Organizations

121. The SVO shall establish a List of Nationally Recognized Statistical Rating Organizations (NRSROs, as specified in this section, to be used to administer the List of Qualified U.S. Financial Institutions. The SVO shall place on the List of NRSROs any credit rating organization that:

- Is registered with the U.S. Securities and Exchange Commission (SEC) as an NRSRO, as that term is defined in the applicable federal statute.
- Has criteria and methodology for assigning credit ratings to banks and nondepository lenders—sometimes hereafter referred to as nonbank financial institutions (NBFIs)—that the SVO has confirmed is consistent with the needs of the NAIC for purposes of the Model Law and which at a minimum:
- Utilizes an analytical framework that assesses the incremental risk of banks and NBFIs (i.e., nondepository lenders) relative to each other and incorporates as criteria in its bank and NBFI methodology the nature and robustness of regulation, access to the central bank for contingent liquidity and the stability of funding.
- Results in the expression of an opinion of the bank's or NBFI's likelihood of default on an LOC obligation and/or long-term debt obligation
- Results in the assignment of a stable credit rating, defined to mean that the NRSRO considers it unlikely that the assigned credit rating would be downgraded within one year under the moderate stress scenario specified in its credit rating criteria.