

Reorganizations under Chapter 11 of the U.S. Bankruptcy Code

82. The SVO will maintain the NAIC Designation of any issuer liability subject to compromise (i.e., any liability of the issuer that has not emerged intact from the reorganization) at **NAIC 6**. Bankruptcy-remote liabilities may be other than temporarily impaired, but may be upgraded from **NAIC 6** to reflect the credit risk of the new obligor, provided the insurance company has recognized a loss as required by *SSAP No. 36—Troubled Debt Restructuring* in a prior year as discussed in this Manual. New securities issued in lieu of the compromised liabilities on emergence from bankruptcy will be reevaluated in line with the credit of the post-bankruptcy entity.

Work-Out or Restructurings Resulting in Modified Terms

83. The guidance in this subparagraph applies whether new securities are issued or not. Whenever an insurance company has agreed to discuss a modification of the terms of an existing obligation, *SSAP No. 36—Troubled Debt Restructuring* is implicated and the event is a material credit event. Reporting a work-out situation to the SVO as soon as practicable after the decision to restructure the transaction is taken, will enable the SVO to work with the insurer to estimate the fair value of the loan and the credit quality of the issuer.

## CREDIT TENANT LOANS

### FILING INSTRUCTIONS

**NOTE:** See “Policies Applicable to Specific Asset Classes” in Part One for policies governing this activity, as well as “Specific Populations of Securities Not Eligible for Filing Exemption” in “Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities” above.

#### Initial Filing Requirements

84. For Bond Lease Based CTLs and Credit Lease Based CTLs, the reporting insurance company shall submit a completed Bond Lease Based or Credit Lease Based CTL Evaluation Form, as appropriate (in either case together with the documentation described in the Evaluation Form), and the lessee’s Audited Financial Statement, unless the lessee is a rated entity.
85. In the case of Acceptable CTL Variants (ACVs), the reporting insurance company shall submit an Audited Financial Statement, Credit Lease Based CTL Evaluation Form (including the documents described in the Evaluation Form) and a separate memorandum identifying and describing the ACV. Any documents that are unique to the transaction by virtue of its being an ACV should be included.

#### Subsequent Filing Requirements

86. For Bond Lease Based CTLs, Credit Lease based CTLs, Multiple Property Transactions (MPTs) and Acceptable CTL Variants, the lessee or the lessee’s guarantor must have been assigned a credit rating by an NAIC CRP or in the event the lessee, or lessee’s guarantor, is not rated by an NAIC CRP, the reporting insurance company shall file the Audited Financial Statement of the lessee or the lessee’s guarantor, as the case may require.

### GENERAL

#### SVO Procedure

87. Upon receipt of an Evaluation Form, the SVO analyst shall first review the Evaluation Form and other documents submitted by an insurer to verify that the transaction reflects appropriate CTL criteria. If the information provided on the Evaluation Form suggests that the transaction is likely to reflect all appropriate CTL criteria, the analyst shall proceed to determine either: (a) the transaction reflects risk consistent with the definition and other criteria for the category; or (b) the transaction contains risks different from those normally associated with Schedule D transactions.

88. Where, in the opinion of the analyst and where otherwise appropriate, the risk presented by the transaction is inconsistent with the definition and other criteria for the CTL category but is consistent with reporting a security with an NAIC Designation, the analyst may reflect the additional risk by adjusting the Designation for the transaction downward and away from the credit rating category assigned to the lessee.

### General CTL Issues

89. The following are the types of general issues that may be relevant to SVO's CTL analysis. The list is not intended to be all inclusive and not all statements may be relevant to each CTL category. Where appropriate, analysts shall consider:

- The extent to which the transaction appears well insulated from the credit risk of the lessor.
- If a Phase I report, or the nature and prior use of the land, indicates a substantial likelihood of preexisting environmental contamination, the extent to which the risk is mitigated may be evidenced by a Phase I or II report, an assumption of that cost by the lessee or other acceptable solution.
- If the lessee's NAIC Designation is less than **NAIC 2**, insolvency risks associated with the lessee may be increased, and all other aspects of the transaction may play an important role in the SVO's analysis.
- A previously unrated lessee or guarantor is eligible for CTL consideration if it presents the information requested in the Evaluation Form.
- While the number of lenders is not limited, there must be equivalency in protection for all lenders.
- While lessor's ownership structure is not limited (i.e., special purpose entity is not required), the SVO may require additional information to assess whether the risks associated with the lessor's ownership structure are mitigated.
- While the transaction may involve a leasehold interest created by an agreement between the owner of the fee interest, the ground lessee, the ground lessor and the remainder man, if any (specifically whether or not the ground lease or estate for years is terminated pursuant to a foreclosure of the note(s) or whether all of the ground lease obligations materially match all of the lessee's obligations under the lease).

- Where casualty insurance for full replacement value is required, it shall be provided by an insurer having a claims-paying rating ability at least equivalent to an **NAIC 2** Designation, or if the lessee shall be rated at least the equivalent of an **NAIC 2** Designation and lessee's GAAP net worth is at least \$100 million at the time of origination, by self-insurance. If the credit rating of a lessee self-insuring falls below an **NAIC 2** Designation equivalent, then the lessee shall obtain adequate casualty insurance from an insurer having a claims-paying ability rating at least equivalent to an **NAIC 2** Designation. Within 90 days of a rating downgrade, insurer shall provide evidence to the SVO that the required insurance coverage has been obtained.
- If the lessee is not assigned an **NAIC 2** Designation or better, and the SVO shall consider it necessary to conclude its analysis, the insurer shall collect and send such additional information explaining the strategic importance of the premises to the lessee's business operations (whatever the nature of the leased premises; e.g., retail, office, warehouse, manufacturing plant).

### Evaluation Form

90. The CTL Evaluation Form shall be deemed to be a part of the documentation submitted by the insurer subject to all pertinent rules of the NAIC and of state insurance departments regarding truthfulness, accuracy and completeness. However, the Evaluation Form is not intended to be a statement of criteria to assist structuring of CTLs. Acceptance of an Evaluation Form by the SVO does not imply that the transaction will be accorded Schedule D treatment. The SVO shall have discretion to vary the terms of the Evaluation Form as experience and prudent analytical judgment may suggest.

<b>BOND LEASE BASED CTLs</b>
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### Definition

91. A Bond Lease Based CTL is a transaction structured around the terms of a Bond Lease. A Bond Lease is a lease between a lessor and a lessee for a specified period of time with specified rent payments that are at least sufficient to repay the related note(s). The Bond Lease requires the lessee to perform all the obligations related to the leased premises. The investment community has historically defined a Bond Lease as a "hell or high water lease," the general concept being that regardless of what occurs as to the leased premises, the lessee is obligated to continue to pay its rent. Therefore, the focus is on the credit of the lessee (or of the guarantor of lessee's obligations) under the Bond Lease, not the real property characteristics related to the premises.



## Legal Characteristics of Bond Leases

92. A Bond Lease reflects the following legal characteristics:

- The lessee is responsible for every obligation related to the leased premises, such as payment of all taxes and utilities, the performance of maintenance, environmental and ground lease obligations (if any) and the obligation that the lessee must indemnify the lessor against losses and claims relating to the leased premises. The lessor's only obligation may be to provide quiet enjoyment of the premises by the lessee.
- The lessor makes no representations or warranties regarding the condition of the leased premises and the lessee accepts the premises "as is."
- The lessee has no right to offset or abate rent or to terminate the Bond Lease upon the occurrence of obsolescence, condemnation, casualty or for any other reasons, except that the lessee may terminate the Bond Lease (a) at any time, if the termination coincides with the lessee's purchase of the leased premises, for an amount at least sufficient to pay the outstanding principal balance and accrued interest; or (b) during a period no longer than the last three years of the lease term without such purchase, in the event of a condemnation and casualty, if the insurance proceeds (or self-insurance proceeds) and condemnation awards are payable to the lender/trustee and are in amounts sufficient to pay the loan in full.
- The lessee is not required to occupy the leased premises if the occupant is a subsidiary or affiliate of the credit tenant. In these cases, the SVO may require additional information regarding the strategic importance of the leased premises.
- The lessee may assign and sublease if the lessee remains unconditionally liable for the performance of all lessee obligations.
- The Bond Lease cannot be amended without the lender's consent.
- The Bond Lease or other relevant document(s) must specifically prohibit a merger of estates.

## Structural Characteristics of Bond Lease Based Transactions

93. A Bond Lease and related documentation reflect the following structural characteristics:

- Payments under the note, including a balloon payment, correspond to a lease payment due from the lessee pursuant to the Bond Lease that is equal or greater than the note payment. The term "balloon" in the definition is intended to imply only a payment larger than previous payments and does not contemplate permitting transactions with refinance risk.
- Neither the lease payments nor the debt payments need be level.

- The lessee is required to pay for all expense items.
- The lessee leases 100% of the real property securing the note.
- There is a valid first lien on the real property or the leasehold estate in favor of the lender/trustee.
- There must be in effect a fully executed irrevocable and perfected assignment of lease payments in favor of the lender/trustee and the lender/trustee must be directly collecting lease payments sufficient to fully pay each and every installment of debt service.
- To the extent the credit to be relied upon is that of a guarantor, the guarantee of the lessee's obligations must be irrevocable and unconditional, and must guarantee performance of all obligations of the lessee under the Bond Lease. The term "guarantor" excludes third-party guarantees for purposes of credit enhancement but is intended to include support arrangements, which in the opinion of the SVO, are entered into as a regular part of the business of the lessee or the group of entities of which the lessee is a part.
- Loan to value is not relevant and therefore not limited.

#### **CREDIT LEASE BASED CTLs**

##### **Definition**

94. A Credit Lease Based CTL transaction is one structured around a Credit Lease. A Credit Lease is a lease between a lessor and a lessee for a specified period of time with specified rent payments at least sufficient to repay the related note(s). The Credit Lease requires the lessee to perform most of the obligations related to the leased premises. A Credit Lease transaction is a corporate bond/commercial mortgage transaction whose primary risk/return characteristics are derived from the creditworthiness of the lessee rather than from the traits of the mortgaged property. The principal difference between a Bond Lease and a Credit Lease is the small set of landlord obligations or real estate risks that must be explicitly addressed through well-recognized mitigation methods discussed in this Manual.

## **Legal Characteristics of Credit Leases**

95. A Credit Lease reflects the following legal characteristics:

- The lessee is responsible for most of the obligations related to the leased premises, such as the payment of taxes and utilities, the performance of maintenance, environmental matters caused by its occupancy and ground lease obligations (if any) and must indemnify the lessor against most losses and claims relating to the leased premises. Any exceptions or other obligations must be addressed through insurance, adjusted debt service coverage ratios or other acceptable mitigants.
- The lessee accepts the leased premises, as evidenced by an estoppel certificate.
- The lessee has limited rights to offset or abate rent related to casualty or condemnation or the failure to perform roof, structural or parking obligations.
- The lessee is not required to occupy the leased premises if the occupant is a subsidiary or affiliate of the credit tenant. In these cases, the SVO may require additional information regarding the strategic importance of the leased premises.
- The lessee may assign and sublease if the lessee remains unconditionally liable for the performance of all lessee obligations.
- The Credit Lease cannot be amended without the lender's consent.
- The Credit Lease or other relevant document(s) must specifically prohibit a merger of estates.

## **Structural Characteristics of Credit Lease Based Transactions**

96. A Credit Lease Based transaction reflects the following structural characteristics:

- Payments under the note, including a balloon payment, correspond to a lease payment due from the lessee pursuant to the credit lease, except that the loan term may exceed the lease term by not more than six months, and the outstanding principal balance at the end of the lease term shall not exceed 5% of the original loan balance.
- Neither the rent payments nor the debt payments need be level.
- The lessee is required to either directly pay or to reimburse the lessor for primary expense items (e.g., taxes, utilities, maintenance and other operating expenses).
- The lessee leases 100% of the real property securing the note.
- There is a valid first lien on the real property or the leasehold estate in favor of the lender/trustee.

- There must be in effect a fully executed irrevocable and perfected assignment of lease payments in favor of the lender/trustee and the lender/trustee must be directly collecting lease payments sufficient to pay the debt service fully.
- To the extent the credit to be relied upon is that of a guarantor, the guarantee of the lessee's obligations must be irrevocable and unconditional, and must guarantee performance of all obligations of the lessee under the Credit Lease. The term guarantor excludes third-party guarantees for purposes of credit enhancement, but is intended to include support arrangements that in the opinion of the SVO are entered into as a regular part of the business of the lessee or the group of entities of which the lessee is a part.
- Loan balance shall not exceed initial appraised value of the property. An appraisal must be done in accordance with Member of the Appraisal Institute (MAI) standards. The value reported in the appraisal report must proceed from a comparison of each of the (a) cost, (b) comparative and (c) income approaches.

### Risks and Acceptable Mitigants in Credit Lease Based Transactions

97. The following are acceptable forms of mitigation against landlord-retained obligations:

- **Roof, Structural and Parking Expenses Not Explicitly Covered by Credit Lease** – (a) Deduct all appropriate costs in calculating an adjusted debt service coverage (DSC) ratio of at least 1.05x; and (b) Provide that funds shall be escrowed in amounts estimated to be accumulated, on a substantially level basis, to a level sufficient to allow for payment of the named costs at the time they are expected to occur.
- **Loan Term Exceeds Initial Lease Term** – (a) Difference shall not exceed six months; and (b) Remaining principal shall not exceed 5% of original loan balance.
- **Casualty** – (a) Rent loss insurance (or an obligation to pay rent regardless of a casualty) is required from an insurer having a claims paying ability rating equivalent to an **NAIC 2** Designation, or self-insurance by a tenant having a credit rating equivalent to an **NAIC 2** Designation, and whose GAAP net worth is at least \$100 million, at the time of the origination; (b) If the casualty does not result in termination of the Credit Lease, proceeds must be used to repair and restore premises; and (c) If the casualty results in the termination of the Credit Lease, awards go to the lender to the extent of the outstanding principal and interest. Termination is only allowed in the last three years of the lease term, unless the lessee is required to make a termination payment at least equal to the outstanding principal and accrued interest.

- **Ground Lease Obligations Not Explicitly Addressed in Credit Lease –** (a) Credit Lease payments must be sufficient to pay ground rent, with DSC adjusted accordingly; and (b) Attornment (non-disturbance) or other agreement between fee owner and lender is required, obligating ground lessor to notify lender of any default by ground lessee and permitting lender an opportunity to cure the default.
- **Condemnation –** (a) Where condemnation results in the termination of the Credit Lease, all awards go to the lender to the extent of the outstanding principal and interest; and (b) Where condemnation does not result in the termination of the Credit Lease, the premises must be repaired and restored.
- **Environmental –** Phase I environmental report showing no environmental problems or, if the Phase I report shows a problem or the nature and prior use of the land indicates a substantial likelihood of preexisting environmental contamination, a Phase II report and an assumption of that cost by the lessee or other acceptable solution.

<b>ACCEPTABLE CTL VARIANTS</b>
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98. An acceptable CTL variant (ACV) is a transaction that meets substantially all of the standards for a Bond Lease Based or Credit Lease Based CTL but that contains one or more of the variants described in the “Guidelines for Acceptable CTL Variants as set forth in this Manual. An insurance company may report an ACV to the SVO by submitting the Bond Lease Based or Credit Lease Based Evaluation Form, whichever is appropriate, specifically identifying the items in the Bond Lease Based or Credit Lease Based CTL standards not present in the submitted transaction, explaining the differing language, device or mitigant put in place to substitute for the missing criteria and providing documentation to substantiate the different approach employed in the transaction.

### **Guidelines for Acceptable CTL Variants**

99. Transactions that exhibit the following variations from the definitions of Bond Lease or Credit Lease Based CTL contained above will nevertheless be eligible for Schedule D treatment in accordance with these guidelines and the definitions if the following standards are met:
- Transactions where lease payments are insufficient to cover required debt service. The shortfall would be covered fully by credit enhancement, cash escrow or excess rent set-asides.

- Transactions with balloon payments in excess of 5% for Credit Lease Based CTLs if lease payments or credit enhancement fund the balloon. The SVO will assess the extent to which the payment stream, whether provided by the lease or credit enhancement, covers the balloon payment.
- Transactions where loan term exceeds lease by more than 6 months. The lessee is obligated either to renew the lease, purchase the property or terminate the lease and pay an amount equal to the outstanding debt. If the tenant renews the lease, the renewal term would have to be for the balance of the loan term. If the tenant purchased the property, the sale and settlement of the landlord's loan obligation must occur not later than the date prior to which lease payments would cease and there must be a simultaneous payment to the lender.
- Transactions that have been purchased by the reporting insurance company from another institution via an assignment. If Bond Lease or Credit Lease criteria are met, the fact that the transaction was acquired through an assignment does not jeopardize CTL treatment.
- Transactions in which the tenant occupies less than 100% of the premises. The reporting insurance company shall identify the credit tenant and the credit tenant's lease payments shall be sufficient to cover the necessary escrow, common area maintenance and other relevant costs.
- Transactions where the user of the property is not affiliated with credit tenant or guarantor. If (a) the credit tenant or a guarantor is liable for and agrees to make the required lease payments and (b) despite lack of affiliation between the parties, there is a substantial community of interests between the parties; e.g., the relationship that might exist between an auto manufacturer and an auto supplier.
- Transactions where the tenant may terminate the lease despite the fact that the amount due under the lease is greater than 5% of the original loan amount. The tenant shall not terminate the lease without first paying off the loan or extending the term of the lease to a term sufficient to amortize the remaining balance of debt.
- Transactions in which the landlord has obligations other than those specified in the definition for Credit Lease Based CTLs. The SVO shall have sole discretion to determine whether the level of risk associated with the retained landlord obligation is consistent with the mitigant used. The SVO anticipates that the reporting insurance company will provide a structure that protects the cash flow. Devices like cash escrow or excess rent set asides may be appropriate mitigants.

- Transactions in which the landlord retains obligations but where the lease requires the tenant to continue to make payments regardless of landlord's breach of these obligations, with tenant's only remedy to pursue legal remedies for damages against the landlord. These transactions would be treated as Credit Lease Based CTLs, irrespective of the fact that the stated variation may be the only difference between the submitted transaction and a Bond Lease Based CTL.
- Transactions that permit lease termination for casualty to all or substantially all of the property prior to the final three years of the lease term. The reporting insurance company must demonstrate that insurance by a third party acceptable to the SVO is in place and fully covers principal and interest in the event of lease termination. A key consideration in this variation is that it be clear that the insurance company lender would always "walk away whole."
- Transactions that permit the lease to be canceled if the property is not restored within a specified time period after a casualty. The transaction shall incorporate a mechanism to assure that the casualty could be repaired within the term of the insurance policy then in force and the mortgagee would have to permit application of insurance proceeds to pay off the debt.
- Transactions in which the tenant has a right to abate rent during a casualty, condemnation, repair or restoration event. The reporting insurance company shall provide: (a) evidence of rent insurance of a duration of at least 1 year from a company rated the equivalent of an **NAIC 1**; and (b) evidence that the tenant is obligated to resume paying rent after the end of the insurance policy payments, regardless of the status of the casualty, condemnation, repair or restoration event.
- Transactions that provide a right to terminate the lease and substitute property on substantial casualty or condemnation. The tenant shall substitute equivalent leased property.
- Transactions where tenant has a right to condemnation award for value of leasehold estate or tenant improvements. If the tenant has a leasehold interest in the premises because it has advanced funds for improvements, CTL eligibility is not affected because the agreement would permit the tenant to receive proceeds of the condemnation award, provided the tenant continues to be obligated to make the payments called for under the lease and those payments are sufficient to pay the loan in full, or the loan is repaid.

- Transactions with an unsatisfactory Phase I or II report. These sections are intended to provide the industry with a device through which it can communicate environmental issues to the SVO. Generally, the SVO anticipates that all CTL transactions will have a Phase I report. If the Phase I report sets forth an unfavorable matter, a Phase II report shall provide more detailed study of the issue. If the reporting insurance company wants to pursue the transaction it may present the Phase II and other material information to the SVO, detailing the manner in which it would mitigate the risk. The SVO would then determine whether the proposed solution serves as an adequate mitigant for the risk.
- Transactions with a stale environmental audit. These transactions may be permitted if the tenant has been in the property since the date of the initial audit, the initial audit is available and acceptable to the SVO and the tenant's use of property is not environmentally sensitive. The documents shall include reliance on a strong net lease paragraph to establish that all environmental obligations are tenant obligations and not landlord obligations.
- Transactions with appraisals submitting only one appraisal method. A transaction may be submitted with an appraisal that lacks all three-valuation methods (cost, comparative and income approaches) if the appraisal is in accordance with MAI standards and makes clear that the other two methods were not applicable and this is stated in the MAI opinion.
- Transactions with second mortgages. Rent must exceed aggregate debt service on all debt up to required Credit Lease Based coverage standards and the second mortgagee could not put lender into default.
- Transactions where the lender is the second mortgagee. Rent must exceed aggregate debt service on all debt up to required Credit Lease Based coverage standards and the lender shall have a right to cure first mortgage defaults.
- Transactions with minor lessor representations, warranties or covenants. Staff shall have sole discretion to assess the nature of the landlord obligation and the extent to which the mitigant is appropriate. However, these transactions may be permitted if the tenant is estopped from asserting these lessor obligations to abate or cease payment of rent, or if there is credit enhancement or other collateral available to protect against tenant non-payment.
- Use of collateral trustee and issuance of trust certificates. The use of a collateral trustee, or trust certificates, has no impact on eligibility for CTL treatment if the transaction continues to be a mortgage loan in scope of SSAP No. 37. Staff will, of course, review appropriate documentation associated with the arrangement.



- Transactions involving a “Dark Store.” The SVO will raise no objection to CTL eligibility for a transaction in which the original lessee “darkens” the leased premises if the lessee remains unconditionally liable for the performance of all lessee obligations.

<b>MULTIPLE PROPERTY TRANSACTIONS (MPTs)</b>
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**Definition**

100. An MPT transaction is a series of single property Bond Lease Based CTLs or Credit Lease Based CTLs (but not both) combined in one transaction. The MPT category does not alter the fundamental structure or principles of either the Bond Lease Based or the Credit Lease Based CTL. To qualify as an MPT CTL, each site or property must satisfy the existing Bond Lease Based or Credit Lease Based CTL definition, on a stand-alone basis.

**General Legal Characteristics of MPTs**

101. An MPT transaction reflects the following legal characteristics:
- Each property or site qualifies as: (a) a Bond Lease Based CTL; or (b) a Credit Leased Based MPT CTL, as defined below.
  - Either: (a) a single credit tenant; or (b) “affiliated” credit tenants with a guarantee by the parent.
  - Differences in the documents are identified and limited to dollar amount of rent or debt and state/local law differences.
  - Local counsel opinion(s) and a special counsel opinion regarding enforceability of documents, perfection of security interests in the collateral and consequently, the recordation of security documents, are provided to the SVO.
  - For Credit Lease Based MPT CTLs, each property has a satisfactory Phase I environmental report and an Appraisal indicating the appraised value of the property and containing the appraiser’s name and certifications done in accordance with MAI standards.
  - Existing cross default and/or cross collateralization provisions are identified.
  - Any variance must be consistent among all the properties or sites in the transaction.

### **Legal and Structural Characteristics of Credit Lease Based MPT CTLs**

102. The legal and structural characteristics of a Credit Lease Based MPT CTL shall be the same as the existing Credit Lease Based CTL definition, with the following modifications:

- There must be a single lessor.
- Either a single credit tenant or affiliated credit tenants with a guarantee by the parent; however, in all cases the lessee must occupy the leased premises.
- Any guarantee of a lessee's obligation must be with respect to all properties in the transaction.
- All risks and acceptable mitigants, as currently described in the existing Credit Lease Based CTL definition, must be uniform for each property.

### **Acceptable CTL Variants Eligible for MPT Treatment**

103. The following Acceptable CTL Variants will be acceptable for Credit Lease Based MPT CTLs:

- Transactions that have been purchased by the reporting insurance company from another institution via an assignment. If Bond Lease or Credit Lease criteria are met, the fact that the transaction was acquired through an assignment does not jeopardize CTL treatment.
- Transactions where the tenant may terminate the lease, despite the fact that the amount due under the lease is greater than 5% of the original loan amount. The tenant may not terminate the lease without first paying off the loan or extending the term of the lease to a term sufficient to amortize the remaining balance of debt.
- Transactions that permit lease termination for casualty to all or substantially all of the property prior to the final three years of the lease term. The reporting insurance company must demonstrate that insurance by a third party acceptable to the SVO is in place and fully covers principal and interest in the event of lease termination. A key consideration in this variation is that it be clear that the insurance company lender would always "walk away whole."
- Transactions that provide a right to terminate the lease and substitute property on substantial casualty, economic obsolescence or condemnation. The tenant would have to substitute equivalent leased property.

- Transactions with appraisals utilizing only one appraisal method (provided that the appraisal method is uniform for all properties). A transaction may be submitted with an appraisal that lacks all three valuation methods (cost, comparative and income approaches), provided the appraisal is in accordance with MAI standards and makes clear that the other two methods were not applicable and this is stated in the MAI opinion.

<b>CTL VARIANTS REQUIRING AN NAIC CRP RATING</b>
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104. An NAIC CRP rating is required for CTL transactions:
- With two credit tenants in the transaction.
  - If lease payments do not commence until completion of construction, but cash escrow or credit enhancement is available during construction sufficient to negate risks.
  - If additional credit enhancement would upgrade the rating of the transaction above the credit rating of the tenant.
  - Where self-insured tenants with a Designation below **NAIC 2** are required to maintain a specified minimum net worth or to immediately obtain insurance.
  - Where environmental issues are not addressed, but there is a strong net lease paragraph, indemnification, compliance with laws or maintenance covenants.
  - With unaddressed and preexisting environmental issues, if there is credit enhancement or other collateral to support the risk.
  - Where there is no appraisal or MAI equivalent. Where landlord makes construction warranties or credit tenant has limited rights to offset rent for construction, if estopped agreements are in place or there is agreement from credit tenant that set-offs are nonbinding against lender because the risk is fully mitigated.

## GROUND LEASE FINANCING TRANSACTIONS

**NOTE:** See “Policies Applicable to Specific Asset Classes” in Part One for policies governing this activity, as well as “Specific Populations of Securities Not Eligible for Filing Exemption” in “Procedure Applicable to Filing Exempt (FE) Securities and Private Letter (PL) Rating Securities” above.

### FILING INSTRUCTIONS

#### Initial Filing Requirements

105. For ground lease financing (GLF) transactions, the reporting insurance company shall submit a complete GLF Evaluation Form together with the documentation described in the GLF Evaluation Form and, if available, evidence of a current Eligible NAIC CRP Rating and related NAIC CRP analysis for: (a) the GLF Transaction (including, but not limited to, rating methodology used, model assumptions and stress test results); and (b) each space lessee or its guarantor or business operator in the case of a hotel, warehouse, intermodal facility, etc., or other business operation.

#### Subsequent Filing Requirements

106. For GLF Transactions, the reporting insurance company shall submit evidence, if available, of a current Eligible NAIC CRP Rating and related NAIC CRP analysis for: (a) the GLF Transaction (including, but not limited to rating methodology used, model assumptions and stress test results); and (b) each space lessee or its guarantor or business operator. For purposes of this section, a current Eligible NAIC CRP Rating is defined as one issued or reviewed within the past 12 calendar months. If the GLF Transaction is modeled by the NAIC’s third-party modeling vendor, the reporting insurance company will submit the data required by the vendor in the form such vendor specifies. In the event a space lessee or its guarantor or the business operator, as the case may be, is not rated by an NAIC CRP and a space lease or business operation is not modeled, the reporting insurance company shall file the Audited Financial Statements and other relevant credit information of the space lessee or its guarantor or business operator, as the case may require, consistent with all corporate bond filing requirements.

### GENERAL

#### SVO Procedure

107. Upon receipt of a GLF Evaluation Form, the SVO analyst shall review the form and all documentation submitted with it and shall proceed with analysis in accordance with section “SVO Approach to GLF Transactions” below.

**DEFINITION AND OVERVIEW****Ground Lease Financing Transaction – Definition and Overview**

108. A ground lease financing (GLF) transaction is in scope of SSAP No. 37 – Mortgage Loans and typically has two components: (a) a ground lease for a long period (e.g., 99 years) between a ground lessor who owns the land and a ground lessee who attains a leasehold for the purpose of developing the land; and (b) the subleasing of space or operation of a business such as a hotel, warehouse, intermodal facility, etc., in an existing or to-be-constructed building to one or more tenants (space tenants) under shorter (e.g., 5–15 year) leases (space leases) or to the operator of a business such as a hotel, warehouse, intermodal facility, etc., under a franchise agreement or other arrangement.
109. Both the ground lessor and ground lessee will typically finance their respective estates (i.e., the fee estate of the ground lessor and the leasehold estate of the ground lessee); (a) the ground lessor, typically, with the issuance of debt-like certificates or notes; and (b) the ground lessee, typically, by borrowing from a financial institution or traditional mortgage lender. To secure the financing, the ground lessor will grant to the lender a mortgage on the fee property such ground lessor owns, and the ground lessee will pledge to the leasehold lender its leasehold estate and its rights under the ground lease and in the improvements which it owns and the space leases if any.
110. Typically, in a GLF transaction neither the ground lessor nor the ground lessee is an entity either: (a) rated by an NAIC CRP; or (b) whose credit worthiness can be evaluated by the SVO. Rather, they are special purpose vehicles (SPVs) intended to be bankruptcy remote.

111. In a GLF transaction, it is often the case that the ground lease (i.e., the first leg of the transaction) is structured with the same attributes as a lease in a CTL transaction (e.g., it is “hell or high water” or “triple net”). However, because the ground lessee is an SPV rather than a corporate entity, there is no NAIC CRP corporate credit rating or SVO corporate analysis to rely on. To determine whether the ground lessee will have sufficient funds to pay its ground lease obligations the SVO must look to the rent payments of the space tenants or the operation of the business conducted in such improvements (such as a hotel, warehouse, intermodal facility, etc.). Depending on the specifics of a GLF transaction, analysis of space leases and space tenants and business operations and business operators could be more akin to a commercial mortgage backed security (CMBS) analysis than the corporate analysis in a CTL transaction because: (a) the space leases may not meet the CTL criteria and can consist of one or several space tenants of differing credit profiles and each with differing space lease terms and ultimate payment on the GLF is dependent on the space tenants making their rent payment on the space leases; or (b) in the event there is a business operation, ultimate payment on the GLF is dependent on the operation of such business to generate cashflow for ground rent and other expenses. For this reason, the SVO may refer certain GLF transaction space lease or business operations analyses to the SSG because of the SSG’s financial modeling capabilities and because, in accordance with this Manual, it analyzes and assigns NAIC Designations to CMBS transaction.

#### **ANALYSIS AND SPECIFIC CONSIDERATIONS**

##### **SVO Approach to GLF Transactions**

112. All GLF transactions are ineligible for filing exemption and must be submitted to the SVO. The SVO will conduct GLF transaction review in the following manner:
- The SVO will analyze the GLF transaction structure and determine whether the ground lease meets the CTL criteria for Bond Lease Based or Credit Lease Based CTLs, except for not having a credit tenant. If the SVO, in its sole discretion, determines the ground lease does not meet the Bond Lease Based or Credit Lease Based CTL criteria, except for a credit tenant, the security would be ineligible for Schedule D reporting.

- If the ground lease meets the CTL criteria, except for a credit tenant, and if three or fewer space tenants, each of which: (a) are rated by an NAIC CRP; or (b) whose credit worthiness can be evaluated by the SVO, when combined comprise ninety percent (90%) or more of the total space tenant lease obligations, the SVO will analyze the space leases to determine if they meet the CTL criteria for one of the four CTL categories in this Manual. If so, the SVO can, in its sole discretion and based on its analytical judgment, analyze the transaction as akin to a CTL, based on the CTL-like nature (e.g., “hell or high water” or “triple net” features) of both the ground and space leases, the limited number of space leases and the corporate credit profiles of the space tenants.
- If the ground lease meets the criteria for Bond Lease Based or Credit Lease Based CTLs and there are four or more space tenants, or the SVO has determined that it cannot apply the approach in (b) above or the transaction does not meet the criteria set forth in (b) above, the SVO will refer the space leases or the business operation, as the case may be, to the SSG for possible financial modeling. If the SSG, in conjunction with its third-party modeling vendor, and in its sole discretion and analytical judgment based on factors including, but not limited to, availability of data, transaction structure and other transaction specific risks, determines that the space leases or business operation can be modeled, it will analyze the space leases or business operation, as the case may be, to determine whether they will provide sufficient cash flow to pay the ground lease rent payments and any additional costs which the ground lessee is required to cover pursuant to the ground lease terms (e.g., taxes, utilities, maintenance, insurance).
- If the SSG, in conjunction with its third-party modeling vendor, and in its sole discretion and analytical judgment, determines that it is unable to model the space leases or business operation, as the case may be, and if the transaction has been assigned a public or private Eligible NAIC CRP Rating the SVO shall proceed with an analysis of the transaction guided by the available analyses of all NAIC CRPs that provided an Eligible NAIC CRP Rating on the transaction. For the avoidance of doubt, the SVO’s analysis will be entirely at the discretion of the SVO and the SVO is not obligated to accept or follow the rating methodology of any NAIC CRP and can, in its sole discretion and based on its analytical judgment, assign an NAIC Designation which differs from the correlated Eligible NAIC CRP Rating or choose not to assign any NAIC Designation. The SVO may, in its sole discretion, upon written request from the submitting investor, disclose its rationale as to why such transaction was not given a Designation correlated to the Eligible NAIC CRP Rating.
- Should the SVO or, if applicable, SSG determine that it cannot assign an NAIC Designation to the GLF, the GLF would be ineligible for Schedule D reporting.

### GLF Specific Considerations

113. The space lease payments or business operation, as the case may be, should be sufficient to cover any recurring costs the ground lessee is obligated to pay (e.g., taxes, utilities, maintenance, insurance) pursuant to the terms of the ground lease. All such ground lessee obligations will be factored into the SSG's financial model of the space leases or business operations, if applicable.
114. To provide comfort that there will be no environmental liabilities, the filing documents shall include a Phase I environmental report showing no environmental problems and, if the Phase I report shows a problem or the nature and prior use of the land indicates a substantial likelihood of preexisting environmental contamination, a Phase II environmental report.
115. Typically, a ground lease will require the ground lessee to hold the following insurance to protect the ground lease payments from potential shortfall due to the termination or abatement of space lease payments or reduction or termination of business operation upon the occurrence of condemnation or casualty or other insurable condition. Any of the insurable risks below that are not insured should be otherwise mitigated and evidence of such mitigation should be included in the filing documents.
- Casualty insurance in an amount of coverage equal to 100% of the replacement value of the improvements with the fee lender named as the loss payee.
  - Rent loss insurance in an amount of coverage equal to at least 12 months of ground rent with the fee lender named as loss payee.
  - General liability insurance. The amount of coverage shall be sized appropriately, depending on the size and type of building (e.g., office, hotel, warehouse, intermodal facility, etc.).
  - Ground Lessor would be required to purchase special risk condemnation insurance in an amount of coverage equal to the principal amount of the GLF. This policy shall be prepaid and remain in place for the entire term of the GLF secured by the fee mortgage.

**NOTE:** All insurance must be issued by a carrier with an NAIC Designation equivalent rating of 1.G or better.



**WORKING CAPITAL FINANCE INVESTMENTS**

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**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” above.

**Initial Filing Requirements**

116. An insurance company requesting an analysis of a proposed Working Capital Finance Program shall provide the SVO with the documentation described in this subparagraph:

- An RTAS Application.
- The Obligor’s Audited Financial Statements, if the Obligor is not rated for credit risk by a NAIC CRP.
- The insurance company’s Investment Committee Memorandum for the proposed Working Capital Finance Program.
- One of the following:
  - An annual independent report according to Statement on Standards for Attestation Engagements (SSAE) No. 16 (or functional equivalent), reporting on controls at a service organization related to the administration of the investment.
  - An annual audit of the financial statement and internal controls of the consolidated group of which the Finance Agent is part, which does not note any material weakness related to servicing working capital finance investments.
  - A Certification from the insurance company’s Investment Officer that the insurance company, in its capacity as an Investor, is not affiliated with the Obligor or with any Supplier in the Working Capital Finance Program, and that the Working Capital Finance Program does not include any insurance or insurance related assets.
- A copy of:
  - The document(s) that create the Working Capital Finance Investments (i.e., the short-term receivables) that is the subject of the RTAS – Emerging Investment Vehicle Service Application, and establishes the obligations of the Obligor to, and the protection afforded owners of, Working Capital Finance Investments (including the Investors). This agreement is sometimes referred to as the Invoice Payment Terms Acknowledgement, the Payable Services Agreement or the Paying Services Agreement.

**NOTE:** Please refer to “The Regulatory Treatment Analysis Service – Emerging Investment Vehicle” in Part Two for guidance regarding the filing of an RTAS Application with the SVO.

- The agreement(s) between the Obligor and the Finance Agent governing the administration of the Working Capital Finance Program and the Working Capital Finance Investments issued thereunder. These agreements may be included in the documents mentioned above or may be a stand-alone agreement which are sometimes referred to as the Settlement Services Agreement or the Invoice-Related Electronic Services Agreement.
- The agreement governing the sale of the Working Capital Finance Investments from the Supplier to the Finance Agent. This agreement is sometimes referred to as the Receivables Purchase Agreement or the Supplier Agreement. The agreement governing the ongoing purchase of Working Capital Finance Investments or an interest in Working Capital Finance Investments by the Investor from the Finance Agent. This agreement is sometimes referred to as the Agency Agreement, the Participation Agreement or the Program Trust Agreement.

### Subsequent Filing Requirements

117. Subsequent filing requirements include:

- Copies of any of the documents originally submitted with the RTAS Application subsequently amended.
- One of the following:
  - An annual independent report according to Statement on Standards for Attestation Engagements (SSAE) No. 16 (or functional equivalent), reporting on controls at a service organization related to the administration of the investment; or
  - An annual audit of the financial statements and internal controls of the consolidated group of which the Finance Agent is part, which does not note any material weakness related to servicing working capital finance investments.

### Definitions in *SSAP No. 105R—Working Capital Finance Investments*

118. Please refer to *SSAP No. 105R—Working Capital Finance Investments*, for the definitions and associated definitional guidance insurance companies must understand and comply with before applying for an NAIC Designation for Working Capital Finance Programs that would permit them to purchase Working Capital Finance Investments.

119. With the exception of the definitions for Dilution Risk and Operational Risk below, the definitions shown below are summaries of those contained in *SSAP No. 105R—Working Capital Finance Investments* intended only to facilitate a discussion and in all cases subordinate to the definitions in SSAP No. 105R.

### Summary of Key Definitions

120. **Confirmed Supplier Receivable** – A receivable sold by a Supplier to a Finance Agent or Investor (or by a Finance Agent to an Investor) under a Working Capital Finance Program designated by the SVO that requires the Obligor to confirm to the Finance Agent or Investor, prior to the sale of the receivable from the Supplier to the Finance Agent or Investor, that it has no defenses to payment of the monetary obligation represented by the receivable against the Supplier and, therefore, no defenses to payment of the same monetary obligation to the Finance Agent and/or Investor after such sale. The confirmation by the Obligor that it has no defenses to payment includes confirmation that the Obligor does not have a right to refuse payment that it may have acquired with respect to underlying commercial trade transaction and that, if it has such a right, it will not assert such defenses against the Finance Agent or Investor.
121. **Dilution Risk** – With respect to any Working Capital Finance Program, dilution risk refers to disputes or contractual provisions that may reduce the amount of the obligation owed by the Obligor to the Supplier under the original receivable or the obligation owed by the Obligor to the Finance Agent and/or Investor under the Confirmed Supplier Receivable. Examples of dilution risk are credit for returns of defective goods or an allegation of fraud, such as that the invoice is not legitimate or is a duplicate invoice.
122. **Finance Agent** – A bank, financial institution, financial intermediary or service provider that facilitates the Working Capital Finance Program that arranges the sale, assignment or transfer of the Confirmed Supplier Receivable to the Investor and administers payment.
123. **Investor** – The insurance company that files the RTAS Application with the SVO in order to obtain an NAIC Designation for a proposed Working Capital Finance Program.
124. **Obligor** – An entity that purchases the goods or services from the Supplier and thereby generates the original supplier receivable—and which Obligor has, or can be designated, **NAIC 1** or **NAIC 2** by the SVO or has been assigned an equivalent credit rating by a NAIC CRP or, if not so designated, the SVO can assign such NAIC Designation, as directed by the VOS/TF pursuant to the “Working Capital Finance Investments (WCFI)” section in Part One of this Manual.

125. **Operational Risk** – With respect to any Working Capital Finance Program, operational risk refers to the combined effect of the procedures and parties employed to implement the program and their responsibility under the documents and to the determination by the SVO of whether these procedures and parties will ensure full and timely performance by the Obligor of the payment obligation to the Investor. An example of an operational risk is the confirmation process employed to verify that the Obligor has no defenses to payment.
126. **Supplier** – The entity that sells the goods or services to the Obligor, obtains a receivable from the Obligor in exchange and subsequently chooses to sell the right to receive the payment associated with the receivable to the Finance Agent or Investor under the terms of a Working Capital Finance Program designated **NAIC 1** or **NAIC 2** by the SVO.
127. **Working Capital Finance Program** – The program created for the Obligor and its Suppliers by a Finance Agent the terms of which permits Suppliers to the Obligor to negotiate the sale of a right to receive payment from the Obligor (which is associated with and evidenced by a receivable) to the Finance Agent or an Investor.
128. **Working Capital Finance Investment** – The right to receive the payment associated with a Confirmed Supplier Receivable purchased by an Investor under a Working Capital Finance Program designated **NAIC 1** or **NAIC 2** by the SVO and is the subject of *SSAP No. 105R—Working Capital Finance Investments*.

**NOTE:** *SSAP No. 105R—Working Capital Finance Investments* imposes reporting and statutory accounting requirements on insurance company investments in Working Capital Finance Investments. Insurance companies are strongly advised to become familiar with *SSAP No. 105R* before filing an RTAS Application with the SVO.

### Direction and Program Parameters

129. The SVO may assign an NAIC Designation to a Working Capital Finance Program that would generate Working Capital Finance Investment that meet the criterion and standards identified in this Section.
130. **RTAS Submission Required** – A request that the SVO assign an NAIC Designation to a Working Capital Finance Program is made by filing an RTAS Application. The RTAS Application is available at [www.naic.org/documents/svo\\_rtas\\_app.pdf](http://www.naic.org/documents/svo_rtas_app.pdf).
131. Upon completion of its risk assessment, the SVO will issue an RTAS Letter indicating a preliminary NAIC Designation; i.e., the NAIC Designation that would be assigned if the Investor enters into a Working Capital Finance Program with a Finance Agent and sought to report it to the SVO.

**NOTE:** A preliminary NAIC Designation cannot be used for statutory reporting purposes.

132. The SVO shall issue a final NAIC Designation to the Investor for the Working Capital Finance Program and the Working Capital Finance Investments generated thereunder upon receipt of fully executed final copies of the required documentation.

### Variations in Structure

133. Working Capital Finance Programs may differ in structure and in the protection afforded the Investor. Structural strength and weaknesses of various structures in such programs will be reflected in the NAIC Designation assigned by the SVO.

### Program Quality

134. The SVO shall only assign an NAIC Designation to Working Capital Finance Programs that can be designated **NAIC 1** or **NAIC 2**. Credit quality is measured by reference to a NAIC CRP credit rating or an NAIC Designation assigned by the SVO. The SVO shall withdraw the NAIC Designation assigned to a Working Capital Finance Program on the date the Obligor's NAIC CRP credit rating or NAIC Designation is downgraded to **NAIC 3** or its NAIC CRP equivalent.

**NOTE:** *SSAP No. 105R—Working Capital Finance Investments* provides that Working Capital Finance Investments generated under a Working Capital Finance Program of an Obligor that falls below the equivalent of **NAIC 1** or **NAIC 2** becomes nonadmitted.

### Process and Methodology

135. An NAIC Designation shall be assigned to a Working Capital Finance Program on the basis of a thorough assessment of credit, dilution, operational and other risks, an assessment of protections provided by operative documents to the Investor and the quality of transaction participants.

### Risk-Assessment Process

136. **Credit Risk** – The NAIC Designation for a Working Capital Finance Program shall be linked to the credit quality of the Obligor, which may be determined by reference to a credit rating assigned by a NAIC CRP or by an NAIC Designation assigned by the SVO. Credit risk is assessed by the SVO analyst in accordance with any permitted methodology set forth in this Manual for corporate obligors.

137. **Dilution Risk** – To achieve an **NAIC 1** or **NAIC 2** Designation, the Working Capital Finance Program must eliminate dilution risk in the Working Capital Finance Investment proposed to be eligible for purchase by the Investor. The terms governing the Investor's Working Capital Finance Investment must eliminate Obligor recourse to its Supplier as a condition to payment of the obligation to the Investor so as to result in an unconditional right to receive payment on a full and timely basis.
138. **Operational Risk** – To achieve an **NAIC 1** or **NAIC 2** Designation, all operational risks shall be identified and assessed. Key participants shall have a NAIC CRP credit rating or an NAIC Designation assigned by the SVO at a level at least that of the Obligor.

### Legal, Structural and Regulatory Considerations

139. Events of default remedies should provide the Investor at least those rights and privileges, unimpaired, of a trade creditor upon default with no Obligor defenses that could cause dilution of principal.
140. The SVO shall verify that either, (i) the Finance Agent is an entity regulated or supervised by a financial regulator in one of the countries in the List of Foreign (non-US) Jurisdictions Eligible for Netting for Purposes of Determining Exposures to Counterparties for Schedule DB, Part D, Section 1, or (ii) payments due the Investor are made directly by the Obligor (a) to the Investor or (b) into an account maintained by a regulated financial institution for the benefit of Investors in the Working Capital Finance Program, and, in either case, the Finance Agent cannot be the beneficiary of such payment.
141. The SVO will verify that the Certification from the insurance company's Chief Investment Officer confirms that the Investor is not affiliated with Obligor and that Working Capital Finance Investment excludes insurance or insurance-related assets.
142. The remedies available to the participants in the Working Capital Finance Program should be expressly identified in the documentation for the Working Capital Finance Investment.
143. Characteristics that shall be present in a proposed Working Capital Finance Investment include, but are not limited to, the following, or a substantial equivalent:
144. *SSAP No. 105R—Working Capital Finance Investments* provides that the documentation governing Working Capital Finance Programs must provide that disputes arising under the agreements shall be submitted to a court of competent jurisdiction in the U.S. or be subject to an alternative dispute resolution process sanctioned by state law. Given the nature of Working Capital Finance Programs, the SVO anticipates that documentation governing Working Capital Finance Investments will be subject to the laws and jurisdiction of the courts of California, Delaware or New York, or a similar legal jurisdiction with significant exposure to sophisticated institutional financial transactions.

145. Events of default must be clearly defined, and provide a mechanism that gives the Investor the ability to pursue collection unfettered by actions taken or not taken by participants such as the Servicer or Trustee, or other named persons performing similar functions.

## INVESTMENTS IN CERTIFIED CAPITAL COMPANIES

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### Definition

146. A certified capital company (CAPCO) is a state-legislated venture capital firm that can be a partnership, corporation, trust or limited liability company, profit or not-for-profit and which may capitalize itself in a variety of ways. Investors who acquire an equity interest or qualified debt instrument from a CAPCO receive state premium or income tax credit.

### Statutory Accounting Guidance

147. Guidance on the accounting for investments in CAPCOs is in INT 06-02: Accounting and Reporting for Investments in a Certified Capital Company (CAPCO) (INT 06-02) located in Appendix B of the NAIC *Accounting Practices and Procedures Manual*.
148. Before a CAPCO security can be filed with the SVO, the reporting insurance company must apply INT 06-02 to the facts of the specific security. It is the insurance company's responsibility to apply Statutory Accounting Guidance for CAPCO Transactions.
149. INT 06-02 requires reporting entities to account and report for investments in CAPCOs consistent with the security or other interest they acquire except for specific guidance on the tax credits. For example, an investor who acquired a bond issued by a CAPCO would follow the accounting guidance for bonds found in *SSAP No. 26R—Bonds* and report the details about the transaction on Schedule D in accordance with the NAIC Quarterly and Annual Statement Instructions. Such securities are assessed using the procedures referenced in regu of this Manual.
150. For an investor who acquired a limited liability partnership interest, the interest would be valued in accordance with the guidance for limited liability partnerships contained in *SSAP No. 48—Joint Ventures, Partnerships and Limited Liability Companies* and reported on Schedule BA in accordance with the NAIC Quarterly and Annual Statement Instructions within the appropriate Joint Venture, Partnership or Limited Liability Company subcategory.
151. Both of the examples cited immediately above would also follow the specific reporting on tax credits found in INT 06-02.

**NOTE:** Nothing in this Manual is intended to modify or interpret INT 06-02, SSAP No. 26R or SSAP No. 48.



## Procedure for Reporting and Filing with the SVO

152. The insurance company should first determine the reporting for CAPCOs indicated by the statutory accounting guidance. This is done by establishing the character of the investment and then applying the appropriate accounting and reporting guidance and to the extent necessary the related procedures in this Manual for Schedule D or Schedule BA assets. If the CAPCO investment is subject to the SVO filing process and does not meet the filing exempt requirements, it should be filed with the SVO. If the SVO disagrees with the insurance company characterization of the investment, it will so inform the insurance company and provide rationale why the SVO believes the company has misapplied or misinterpreted the guidance of INT 06-02 and request a re-filing if necessary.

## Required Documentation

153. **Unrated** – In the case of a CAPCO issue that is not rated by an NAIC CRP:
- **Initial Filings** – The reporting insurance company completes an SAR and attaches the issuer's public offering statement or private placement memorandum, as the case may be, the insurance company's internal credit committee memorandum and the Audited Financial Statement of the issuer for the last three consecutive years. If an issue is rated by a rating organization other than an NAIC CRP, submit evidence of such rating. If none of these documents are available, the reporting insurance company must obtain and complete the SVO's VIM form and submit it with the required documents and attachments.
  - **Subsequent Filings** – For CAPCO issues that are not filing exempt follow the procedures that apply to Corporate Issues not Filing Exempt to file an annual update with the SVO. The reporting insurance company shall annually file an updated Audited Financial Statement.

## Applicable Methodology

154. The SVO shall have discretion to apply any credit assessment methodology or any combination of credit assessment methodologies to assess the credit quality or assess asset classification of a CAPCO security.
155. The SVO shall have discretion to apply any credit assessment methodology or combination of methodologies and shall consider whether the procedure applicable to securities that contain other non-payment risk should be applied.