NAIC SVO's Regulatory Treatment Analysis Service

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In addition to monitoring the solvency of insurers as an important consumer protection, state insurance regulators also monitor the general insurance and financial markets in which their insurers participate and are impacted. The NAIC Securities Valuation Office (SVO) aids in both of these monitoring processes. A fundamental aspect of the financial solvency function is to provide guidance on the regulatory perception of risks in investment securities to insurance companies and their investment advisors. This helps insurance companies incorporate into their investment decisions an understanding of applicable regulations, and helps ensure that financial markets are not adversely impacted by the formulation of, or subsequent changes in, regulation.

The SVO conducts the day-to-day credit quality assessment and valuation of certain securities owned by the state-regulated insurance companies. The function now performed by the SVO was initiated in 1907. Valuations were initially performed by the state insurance departments themselves and then by Moody's Investors Service under contract to the National Convention of Insurance Commissioners (as the NAIC was then known) until 1942. The SVO, as a distinct staff function of the NAIC, was created in 1943 and assigned the valuation and risk-assessment function it still performs for certain securities today.

Among the many services performed by the SVO on an ongoing basis, the SVO mainly serves to provide designations for any securities that are not rated by a credit rating provider (CRP)—i.e., any one of the major credit rating agencies—after that security has been purchased and filed by an insurance company. Insurance companies report ownership of securities to the Capital Markets and Investment Analysis Office when such securities are eligible for filing on Schedule D or Schedule DA of the NAIC financial statement blank; and life and fraternal insurers may also report certain Schedule BA assets thought to have fixed-income characteristics.

The SVO component of the Capital Markets and Investment Analysis Office conducts credit analysis on these securities for the purpose of classifying the security, and, if deemed to be fixed-income like, assigning an NAIC designation and, in certain cases, also assigning a unit price. These designations and unit prices are produced solely for the benefit of NAIC members (the regulators) who should interpret them from the overall perspective of the specific insurance company and its financial condition.

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However, an increasingly important service for the SVO is the evaluation of a security before it is purchased by or sold to an insurance company. This service allows the insurer to know in advance the likely regulatory treatment of an investment security, its impact on risk-based capital, as well as how it is to be reported for statutory accounting purposes. Anyone may request a pre-purchase evaluation of a new investment security under the SVO's Regulatory Treatment Analysis Service (RTAS).

The RTAS process is intended to permit the SVO to give insurance companies (or any interested person) an assessment of how an investment is likely to be treated by the NAIC under the existing regulatory framework. It permits insurance companies and other persons to ascertain the analytical position the SVO would take (or the recommendations it would make to regulators) with respect to credit and other investment risks embedded in a security and the regulatory treatment that corresponds to those analytical conclusions under the existing regulatory framework. However, it is important to note that an RTAS does not relieve an insurer from any filing requirements once the investment is purchased.

An RTAS application can be accessed via the NAIC website. The documentation required is basically the same as for any first-time filing, and the turnaround time is typically two weeks to a maximum of four weeks after receipt of all of the necessary information. An RTAS may be filed by bankers, fund sponsors, exchange-traded fund (ETF) sponsors or the company that is looking for the rating. Almost any financial advisor may apply on behalf of his/her client. In addition, the cost for this service is quite modest compared to CRP alternatives.

The RTAS service has been popular with bond ETFs and mutual fund sponsors in order to obtain a bond classification, as well as a designation. The RTAS service has also been actively used by new issuers of private placements that do not have, or do not need, an agency rating and only need an NAIC rating to sell their securities to insurance companies. First-time European issuers of private placements have also quite actively sought this advanced rating, as the European bank market has become restrictive, and the companies seek to enter the U.S. private placement market.

Additional information about the RTAS process can be found in the *Purposes and Procedures Manual of the NAIC Securities Valuation Office* or by contacting Harry Olsen at 212-386-1925 or *HOlsen@naic.org.*

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The National Association of Insurance Commissioners (NAIC) is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC staff supports these efforts and represents the collective views of state regulators domestically and internationally. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S. For more information, visit www.naic.org.