

**Sl. No 163**

5. When SSAP No. 105 was developed, SSAP No. 20 was amended to allow working capital finance investments as admitted assets to the extent they conform to the requirements of SSAP No. 105 (see Relevant Statutory Accounting). Some of the WCFI program requirements are to provide protections that help to distinguish these programs from factoring, forfaiting, invoice discounting and other similar programs which have been historically nonadmitted in SSAP No. 20. SSAP No. 105 details that eligible confirmed supplier receivables must not: include insurance or insurance related assets; be impaired or in default at the time of purchase; or have a maturity longer than one year from the date of invoice. In addition, there are restrictions that preclude admission of affiliated WCFI investments.

6. SSAP No. 105 provides that working capital finance investments represent a confirmed short-term obligation<sup>1</sup> to pay a specified amount owed by one party (the obligor) to another (typically a supplier of goods), generated as a part of a working capital finance investment program currently designated by the NAIC Securities Valuation Office (SVO). Pursuant to the long-term working capital finance investment program, a short-term obligation has been transferred by the entity entitled to payment (typically a supplier of goods) to a third-party investor.

7. Working capital finance investments held by a reporting entity represent a right for the reporting entity to receive future payments. This issue paper provides details on the updates to the SSAP No. 105 accounting and reporting guidelines for the right to receive payment under working capital finance programs that meet particular criteria.

## **B**

8. SSAP No. 105 requires an SVO program designation of NAIC 1 or NAIC 2 (See definitions in relevant statutory accounting) in order to admit working capital finance investments. This was an intentional choice by the Working Group and the Valuation of Securities (E) Task Force during the initial development of guidance in 2012 to limit the admissibility to high quality receivables (1 a(ofngrentHo htailydih( )5.5 7.8 (u 22.115 d7dp )T6-

**DISCUSSION**

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12. SSAP No. 105 was originally effective in 2014 and was controversial as it was developed at the request of a single life entity. At that time, some Working Group members objected to the development of a new SSAP, reporting changes and specific asset class

obligor without the rated parent being a guarantor of the unrated subsidiary's WCFI obligations. This aspect envisions the rated entity having some of its own obligations in the program

- ii. Credit Substitution of rated obligor for its unrated subsidiaries which are key transaction participants, but not obligors. The industry proposal was to create criteria to allow the "program" to obtain an acceptable NAIC designation by evaluating if the unrated "key transaction participant" is able to perform its functions. Industry proposed several different ways to attribute the rated entity's credit rating to the unrated entity including:
  - (a) Documented operational control of unrated obligor, or
  - (b) An important inter-relationship with unrated obligor, or
  - (c) If the unrated key transaction participants are reasonably expected to perform their functions.
- d. Change Reporting Schedule - The Working Group did not change the reporting requirements to move the WCFI investments from Schedule BA – Other Assets, to Schedule DA – Short term Investments.

19. Some of the discussion points that were discussed which resulted in the Working Group not directing the inclusion of four of the industry proposed revisions were as follows:

- a. Possible Domestic Regulator Approval – The statement that the reporting entity may need to seek approval from the domestic regulator was maintained as previously noted in Issue Paper No. 147. The Issue Paper documents the possible requirement for domestic regulator approval was an intentional decision because of concerns regarding the ability of smaller entities to monitor the investments in such programs on an ongoing basis.
  - i. It was also noted that the current guidance in SSAP No. 105 is not an explicit requirement, but only identifies that a domiciliary commissioner ~~m~~ require a company to receive initial permission (see final action in paragraph 23).
  - ii. The agenda item noted that the industry proposal noted:
    - (a) that these investments may not fit into the normal investment law categories.
    - (b) the asset class is not for most insurers as it requires relationships with finance agents beyond the traditional dealer insurer.
    - (c) the investor needs specialized knowledge, asset management operations and the ability to book and supervise the assets.
    - (d) the filing fees require sizable commitments to justify the costs, which would make it cost prohibitive for smaller players.
  - iii. As a counterpoint to the decision not to change the guidance in the SSAP No. 105, the Fall 2019 industry comments noted that state approval is not a practical risk mitigant. In addition, the speaker present at the meeting commented that he questioned the evaluation criteria that would be used by a state.

- b. Only High-Quality Obligor – The current requirement which restricts designations of programs and obligors to being of high quality was maintained. The Working Group was not in favor of lowering the credit quality of the acceptable obligors from NAIC 1 (highest quality) and NAIC 2 (high quality) to allow NAIC designations of 3 (medium quality) and NAIC 4 (low quality) (See definitions in relevant statutory accounting).
  - i. The descriptions of NAIC designations in the

RBC charges based on program designation would not be functional if the reporting was moved to Schedule DA, because that schedule does not include designations which are needed for RBC.

#### **Revisions to SSAP No. 105:**

20. On December 7, 2019, the Working Group exposed substantive revisions to SSAP No. 105 to incorporate industry revisions to program requirements, as previously directed by the Working Group during the 2019 Summer National Meeting.

21. The substantive revisions to SSAP No. 105 that were exposed for comment reflected the following elements:

- a. Functionally Equivalent Foreign Regulators - Removed the requirement that the SVO determine if the International Finance Agent is the functional equivalent of the U.S. Regulator. Removing this element was supported by the SVO, which noted that determining functional equivalence is not an analytical issue.
- b. Commingling Prohibitions - Removed the finance agent prohibitions on commingling. Removal of this requirement was supported by the SVO. SVO staff noted if commingling were not a requirement it would consider commingling risk, when present, as a structural deficiency and balance it against the requirement that the Finance Agent be NAIC 1 or NAIC 2.
- c. Investor Rights Edit - Removed duplicative text regarding exercise of investor rights. This revision was to improve readability and eliminate redundancy.
- d. Requirements for filer to Certify Perfected Interest – Removed requirements, with revisions allowing the SVO to determine if a first priority perfected interest in accordance with uniform commercial code (UCC) requirements for each annual submission has been obtained. In deciding to make this revision the following key points were deemed relevant:
  - i. It was noted that the SVO staff has indicated that UCC first priority perfected interest criteria are typically determined when contracting a program and similar objectives can be accomplished in more ways than the UCC lien process. Requiring the UCC lien process was viewed as overly prescriptive.
  - ii. The definition in SSAP No. 105 of a confirmed supplier receivable requires a first priority perfected interest and, SVO analytical staff should be able to determine if first priority interest has been achieved
- e. Finance Agent Validation Requirements – The independent review requirements were broadened to allow independent review of the finance agent by either audit or through one of two types of internal control report. This is a lower threshold, than the existing requirements, but one that still provides some type of independent program review.
- f. Default Date - Changed the default provisions from 15 to 30 days so the default date and the cure period are consistent. This has the effect of changing the date of nonadmission for an investment in default for a period up to 30 days instead of up to 15 days. Key discussion points are:
  - i. Waiting 30 days for a short-term asset can be material in relation to the life of the asset.

- ii. Fifteen (15) days was previously chosen to be consistent with settlement guidance in SSAP No. 21—Other Admitted Assets, which nonadmits and reclassifies receivables for securities not settled within 15 days.
- iii. The “cure period” on confirmed supplier receivables is not to exceed 30 days, therefore, the Working Group agreed that it may make sense for the default date and the end of the cure period to be consistent.

22. At the 2020 Spring National Meeting, the Working Group reviewed the issue paper and the January 2020 comments on the exposed item. Comments received from industry advocated for inclusion of the four items that the Working Group opted to exclude from the additional revisions to the revised Statement. Key elements noted in the industry comments included the following:

- a. Absent all 10 of the industry proposed revisions, investments in working capital finance programs will remain low.
- b. Industry advocated that its proposed credit substitution mechanism to allow unrated subsidiaries was suitable for NAIC implementation to allow not only lower rated subsidiaries but also un-rated subsidiaries. The commenters maintained that the absence of mention of non-rated subsidiaries as acceptable obligors, did not preclude them from allowing unrated obligors. However, the current SSAP No. 105 program requirements explicitly require obligors to be of high credit quality,
- c. The industry comments advocated that lower rated investments should be allowed as the as statutory risk-based capital requirements reflect investment quality decisions in capital calculations.
- d. The industry comments advocated that domiciliary regulator prior approval for investment is a transfer of transaction review from staff to state insurance departments. The commenters noted that when, if regulators ar

- b. This modification was part of the original



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

**SCOPE OF STATEMENT**

1. This statement establishes statutory accounting principles for working capital finance investments held by reporting entities. This statement amends ~~SSAP No. 20—Nonadmitted Assets~~ (SSAP No. 20) to allow working capital finance investments as admitted assets to the extent they conform to the requirements of this statement.

**SUMMARY CONCLUSION**

2. Working capital finance investments represent a confirmed short-term obligation<sup>1</sup> to pay a specified amount owed by one party (the obligor) to another (typ

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undertaking nor that it will not protest, delay, or deny, nor offer nor assert any defenses, personal or otherwise, against payment to the supplier or any party taking claims, interests, or rights to payments made by the supplier.

- a. The confirmed supplier receivable must be sold, assigned or otherwise transferred in a manner that results in an absolute, irrevocable and legally enforceable obligation that has been confirmed by the Obligor.
- b. In the case of a participation, the certificates or other evidence of participation provide an absolute, irrevocable, and legally enforceable obligation of the finance agent or holder of the confirmed supplier receivable to pay to the reporting entity investor all of the amounts due to it under the confirmed supplier receivable, without reduction or delay arising from any claims that the finance agent may have against the reporting entity investor. ~~The reporting entity investor's ability to exercise its rights as creditor, or to direct the finance agent to exercise the rights of a creditor on its behalf, shall not be subject to the discretion of the finance agent or other lenders or investors.~~ The reporting entity investor's ability to exercise its rights as creditor, or to direct the finance agent to exercise the rights of a creditor on its behalf, shall not be subject to, other than during a cure period not to exceed thirty days, the discretion of the finance agent or other lenders or investors.

### CIRP

12. In the case of a purchase, the investor shall verify, prior to the sale that the obligor has confirmed the respective amounts, payment dates and related invoice numbers' specified dates and has waived all the suppI1 Tuan. d(In the case ofll ) f y a l e t h a t t h e o b l i g o r e s s

~~investor must be able to demonstrate the basis for such belief to a regulator or to the SVO upon either's request. Commercially reasonable belief shall mean the SVO deems the investor's belief reasonable in light of the systems, policies, and practices commonly recognized in the field of investing in securitizations, loan-backed, structured, or trust issued securities.~~

#### **PrRip**

~~16.14.~~ The working capital finance program investor must provide in its annual filing with the Securities Valuation Office ~~an annual audit of the consolidated financial statements of which the finance agent is part, which does not report any qualifications related to servicing, and~~ one of the following:

- a. 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
- b. 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 weaknesses related to servicing working capital financial investments.

The NAIC Securities Valuation Office would review the materiality of the report findings in making their determination of the assignment of a designation.

~~17.15.~~ If the credit rating of the working capital finance program or obligor falls to non-investment grade (below the equivalent of NAIC designation "1" or "2"), the reporting entity shall nonadmit, the working

- b. Forfaiting: the purchase of one or a series of receivables from exporters by a forfaiter to enable the exporter (seller) to finance a commercial transaction with a buyer in which the Obligor has no relationship with or contractual obligation to pay the forfaiter and retains all legal defenses to pay it may have against the seller; or
- c. Invoice discounting: the advancement of funds by a finance company to a business entity with the funds advanced limited to a defined percentage of the business entity's eligible and outstanding receivables.

~~21.~~19. Eligible Confirmed Supplier Receivables must not:

- a. Include insurance or insurance related assets;
- b. Be impaired or in default at the time of purchase;
- c. Have a payment (maturity) date longer than one year from the date of the invoice from the Supplier to the Obligor giving rise to the confirmed supplier receivable, and the maturity date must not be subject to change or rolling; nor
- d. Include any receivable of any parent or affiliate of the reporting entity investor, and neither the Obligor nor any Supplier may be affiliated with the reporting entity investor. Working Capital Finance Investments that have obligors or vendors that are affiliated with the investor are ineligible, and therefore, nonadmitted assets.

~~21.~~20.

The right to receive payment generated by a working capital finance investment issued under a working capital finance program is considered to meet the definition of an asset as defined in SSAP No. 4—~~Assets and Nonadmitted Assets~~ is an admitted asset to the extent the investment conforms to the requirements set forth in this Statement and the Purposes and Procedures Manual of the NAIC Investment Analysis Office

shall be reported as net realized capital gains or losses in the statement of income. For reporting entities not required to maintain an AVR, unrealized gains and losses shall be recorded as a direct credit or charge to unassigned funds (surplus).

26.24. A Working Capital Finance Investment may provide

- b. Concentrations of credit risk in accordance with SSAP No. 27—Off-Balance-Sheet and Credit Risk Disclosures (SSAP No. 27) in the annual audited statutory financial reports only.
- c. Information regarding the aggregate book/adjusted carrying value of working capital finance investment by designation including gross assets with nonadmitted and net admitted amounts annually. (Note that programs designated 3-6 are nonadmitted.)

	Gross Asset CY	Non-Admitted Asset CY	Net Admitted Asset CY
WCFI Designation 1			