

SVO



NAIC
NATIONAL ASSOCIATION OF
INSURANCE COMMISSIONERS

TO: Carrie Mears, Chair, Valuation of Securities (E) Task Force
Members of the Valuation of Securities (E) Task Force

FROM: Charles A. Therriault, Director, NAIC Securities Valuation Office (SVO)
Marc Perlman, Managing Investment Counsel, NAIC Securities Valuation Office (SVO)

CC: Eric Kolchinsky, Director, NAIC Structured Securities Group (SSG) and Capital Markets Bureau

RE: Proposed amendment to the Purposes and Procedures Manual of the NAIC Investment Analysis Office (the “P&P Manual”) to add Spain to the list of jurisdictions eligible for counterparty exposure netting

DATE: April 8, 2024

Summary –

Banco Bilbao Vizcaya Argentaria, S.A. (“BBVA”), a bank organized under the laws of the Kingdom of Spain, has requested the addition of Spain to the P&P Manual’s list of jurisdictions eligible for counterparty close-out netting.

The purpose of identifying jurisdictions eligible for close-out netting is to permit the calculation of credit risk exposures to counterparties in Schedule DB, Part D, Section 1. The netting of offsetting liabilities with a counterparty will only be permitted in that Schedule if there exists a master agreement that provides for such netting and if there is adequate legal certainty that closeout netting would be enforced upon default of the counterparty. The P&P Manual provides for the addition of jurisdictions to the list of jurisdictions eligible for close-out netting if, in the SVO’s opinion, legal opinions and/or other analysis provides adequate legal certainty that, upon default of the counterparty, closeout netting would be enforced.

In support of its application, BBVA submitted a legal opinion of the law firm Clifford Chance, S.L.P. on the validity and enforceability of close-out netting provisions under Spanish law. The opinion was commissioned by the International Swaps and Derivatives Association (ISDA), a private trade organization whose mission is to foster safe and efficient derivatives markets, in part through the development of standardized documentation. ISDA netting opinions are widely and accepted by regulators around the globe, specifically by banking regulators.

Each of the netting opinions commissioned by ISDA, including the Spanish opinion, spell out various

parameters, specific to the laws of the relevant jurisdiction, which a master agreement must meet to be consistent with the opinion. For example, according to the Spanish opinion, there are different requirements for netting enforceability depending on whether the insolvent Spanish counterparty is or is not a Spanish bank, credit institution, investment firm or broker dealer. It would be impracticable to expect the SVO to review all master agreements for compliance with the parameters delineated in the netting opinion for the relevant jurisdiction. Therefore, we propose amending the netting eligibility section of the P&P Manual to include a proviso that it is assumed that each master agreement complies with the parameters delineated in the netting opinion for the relevant jurisdiction.

Upon its review of the Spanish law opinion, the SVO has determined that it provides adequate legal certainty that closeout netting would be enforced (assuming, that master agreement provisions are consistent with the parameters explained in the netting opinion) and proposes adding Spain to the list of jurisdictions eligible for counterparty exposure netting.

Proposed Amendment - The proposed text changes to the P&P Manual are shown below with additions in red font color and deletions in ~~red-strikethrough~~, as it would appear in the 2023 P&P Manual format.

PART TWO
OPERATIONAL AND ADMINISTRATIVE INSTRUCTION
APPLICABLE TO THE SVO

COUNTERPARTY EXPOSURE; NETTING ELIGIBILITY

...

Netting Eligibility

...

139. The VOS/TF has determined that there is adequate legal certainty to permit netting of exposures for counterparties domiciled within the United States. Netting of exposures for a foreign (non-U.S.) counterparty will be permitted if its domiciliary jurisdiction has been approved for listing in the List of Jurisdictions Eligible for Netting. Other jurisdictions may be added to the List of Jurisdictions Eligible for Netting if, in the opinion of the SVO, after consultation with the VOS/TF, legal opinions or analyses provide adequate legal certainty that upon default of the counterparty, close-out netting would be enforceable. The SVO's opinion of adequate legal certainty is based on the assumption, authorized by the VOS/TF, that each master agreement will comply with any parameters delineated in the netting opinion for its relevant jurisdiction.

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LIST OF FOREIGN (NON-U.S.) JURISDICTIONS ELIGIBLE FOR NETTING FOR PURPOSES OF DETERMINING EXPOSURES TO COUNTERPARTIES FOR SCHEDULE DB, PART D, SECTION 1

Procedures for Determining NAIC Designations and Netting Eligibility for Derivate Instrument Counterparties

146. **Netting Eligibility** – The purpose of identifying jurisdictions eligible for netting is to permit the calculation of credit risk exposures to counterparties in Schedule DB, Part D, Section 1. The netting of offsetting liabilities with a counterparty will only be permitted in this Schedule if there exists a master agreement that provides for such netting and if there is adequate legal certainty that closeout netting would be enforced upon default of the counterparty.
147. **Legal Certainty for Netting Eligibility** – There is adequate legal certainty to permit netting of exposures for counterparties domiciled within the United States. Netting of exposures in Schedule DB, Part D, Section 1 will be permitted for a foreign (non-U.S.) counterparty if its domiciliary jurisdiction appears on the list in this subparagraph. Jurisdictions will appear on the list if, in the opinion of the SVO, legal opinions and/or analyses provide adequate legal certainty that upon default of the counterparty, closeout netting would be enforced. The SVO's opinion of adequate legal certainty is based on the assumption, authorized by the VOS/TF, that each master agreement will comply with any parameters delineated in the netting opinion for its relevant jurisdiction.

Jurisdiction

Australia

Belgium

Canada

Cayman Island

England

France

Germany

Ireland

Japan

Scotland

Singapore

Spain

Switzerland

https://naiconline.sharepoint.com/teams/SVOVOSTaskForce/Shared Documents/Meetings/2024/2024-05-02 VOSTF Interim Meeting/04-Spain Netting/2024-004.08 P&P_Spain_Netting.docx