

Draft date: 2/10/25

Virtual Meeting

**JOINT MEETING OF THE PROPERTY AND CASUALTY RISK-BASED CAPITAL (E) WORKING GROUP
AND CATASTROPHE RISK (E) SUBGROUP**

Tuesday, February 18, 2025

12:00 – 1:00 p.m. ET / 11:00 a.m. – 12:00 p.m. CT / 10:00 – 11:00 a.m. MT / 9:00 – 10:00 a.m. PT

ROLL CALL

PROPERTY AND CASUALTY RISK-BASED CAPITAL (E) WORKING GROUP

Tom Botsko, Chair	Ohio	Melissa Robertson	New Mexico
Wanchin Chou, Vice Chair	Connecticut	Ni Qin	New York
Charles Hale	Alabama	Will Davis	South Carolina
Rolf Kaumann/Eric Unger	Colorado	Miriam Fisk	Texas
Jane Nelson	Florida	Adrian Jaramillo	Wisconsin
Sandra Darby	Maine		

NAIC Support Staff: Eva Yeung

CATASTROPHE RISK (E) SUBGROUP

Wanchin Chou, Chair	Connecticut	Alexander Vajda	New York
Virginia Christy, Vice Chair	Florida	Tom Botsko	Ohio
Rolf Kaumann/Eric Unger	Colorado	Andrew Schallhorn	Oklahoma
Travis Grassel	Iowa	Will Davis	South Carolina
Sandra Darby	Maine	Miriam Fisk	Texas
Melissa Robertson/Elouisa Macias	New Mexico		

NAIC Support Staff: Eva Yeung

AGENDA

1. Hear Updates from the Wildfire Model Review Ad Hoc Group Regarding the CoreLogic Wildfire Model Review—*Virginia Christy (FL)*
2. Hear Updates on Wildfire Impact Analysis—*Wanchin Chou (CT)*
3. Discuss Wildfire Modeled Losses Impact Analysis— *Wanchin Chou (CT)*
4. Discuss Climate Impact Disclosures—*Wanchin Chou (CT)*
5. Discuss Flood Peril—*Wanchin Chou (CT)*

- a. Federal Emergency Management Agency (FEMA) National Risk Index (NRI) Dataset, Climate Risk Index, and Private Flood Market
 - b. Another Panel Discussion in Summer
6. Hear Updates from the American Academy of Actuaries (Academy) on its current Underwriting Risk Projects—*Ronald Wilkins (Academy)*
 7. Consider Exposure of the Statutory Accounting Principles Working Group (SAPWG) Referral on the Capital Notes and Non-Bond Debt Securities—*Dale Bruggeman (NAIC)*
 8. Discuss Any Other Matters Brought Before the Working Group—*Tom Botsko (OH)*
 10. Adjournment

Attachment A

MEMORANDUM

TO: Tom Botsko, Chair of the Property & Casualty Risk-Based Capital (E) Working Group
Wanchin Chou, Vice-Chair of the Property & Casualty Risk-Based Capital (E) Working Group
Steve Drutz, Chair of the Health Risk-Based Capital (E) Working Group
Matthew Richard, Vice-Chair of the Health Risk-Based Capital (E) Working Group

FROM: Dale Bruggeman, Chair of the Statutory Accounting Principles (E) Working Group
Kevin Clark, Vice-Chair of the Statutory Accounting Principles (E) Working Group

DATE: November 19, 2024

RE: SAPWG Referral for RBC Assessment for Capital Notes and Non-Bond Debt Securities

On November 17, 2024, the Statutory Accounting Principles (E) Working Group adopted INT 24-01: Principles-Based Bond Definition Implementation Questions and Answers to provide application guidance to certain investments in accordance with the adopted bond definition. This adopted INT includes guidance for the classification of certain investments, primarily those issued by banks and treated as capital by banking regulators similarly to how insurance regulators treat surplus notes, as capital notes in scope of *SSAP No. 41—Surplus Notes*. Although the guidance for capital notes in *SSAP No. 41* is not new, it is anticipated that limited investments have been previously reported under those guidelines, as those investments were likely reported as bonds prior to the adopted principles-based bond definition.

Comments received (see attached) in the review of INT 24-01 identified that property & casualty and health companies do not have the ability to receive more granular RBC for capital notes, whereas life companies have the ability to report ratings from credit rating providers (CRPs) for held capital notes to influence RBC. These comments noted that by classifying certain debt securities as capital notes, which are reported on Schedule BA, the RBC impact for P&C and health companies would impose an onerous capital requirement on a highly rated instrument. Note that this dynamic already exists for surplus notes. These comments requested this matter to be reviewed, and that P&C and health insurers be able to follow the provisions permitted by life companies for capital notes reported on Schedule BA.

In considering these comments, the Statutory Accounting Principles (E) Working Group did not incorporate any revisions prior to the adoption of the INT, as investments shall be accounted and reported based on the applicable statutory accounting guidance, regardless of the resulting RBC charge. The Working Group did agree to send a referral to the P&C and Health RBC Working Groups to inform of the comments and to allow for the RBC Working Groups to consider whether modifications should be incorporated into the RBC formula accordingly.

Although the specific comment was focused on capital notes, the Statutory Accounting Principles (E) Working Group has also identified that differences also exist in the calculation of RBC for non-bond debt securities that will be reported on Schedule BA after the principles-based bond definition becomes effective on January 1, 2025. If RBC consistency by type of insurer is desired, consideration may be appropriate for both capital notes and non-bond debt securities.

- Capital Notes & Surplus Notes: Life insurers with investments reported as held capital notes or surplus notes on Schedule BA are permitted to report these investments with CRP ratings. Items reported with CRP ratings result with RBC that corresponds to the bond factors.
- Non-Bond Debt Securities: Life insurers that report non-bond debt securities on Schedule BA are permitted to report these investments with an SVO-Assigned designation. Items reported with SVO-Assigned designations flow through AVR similar to a bond with a corresponding NAIC designation. For these investments, only SVO-Assigned designations are permitted, and ratings received from credit-rating providers cannot be used in allocating the investment through AVR.

The Working Group appreciates your time and consideration of this referral, recognizing that any changes for the RBC of P&C and Health companies is strictly within the purview of the RBC Working Groups. If you have any questions, please contact Dale Bruggeman, or Kevin Clark, SAPWG Chair and Vice Chair, with any questions.

Cc: Julie Gann, Robin Marcotte, Jake Stultz, Jason Farr, Wil Oden, Eva Yeung, Maggie Chang, Kazeem Okosun; Derek Noe

Attachment: Comment Letter Dated Oct. 28, 2024 from Spectrum Asset Management, LLC

[https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/Stat_Acctg_Statutory_Referrals/2024/SAPWG to PCRBC and HRBC - Bonds - 11-18-24.docx](https://naiconline.sharepoint.com/teams/FRSStatutoryAccounting/Stat_Acctg_Statutory_Referrals/2024/SAPWG%20to%20PCRBC%20and%20HRBC%20-%20Bonds%20-%2011-18-24.docx)

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October 28, 2024

Mr. Dale Bruggeman, Chairman
Statutory Accounting Principles (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

RE: Comments on *Principles-Based Bond Definition Implementation Questions and Answers* (Last Updated: October 2, 2024)

Dear Mr. Bruggeman:

Thank you for the opportunity to provide comments on the *Principles-Based Bond Definition Implementation Questions and Answers* document dated October 2, 2024, during the NAIC National Meeting in Denver with comments due October 28th. Please note that our comments reflect our opinion only.

Regarding the “Implementation Questions and Answers” document, section 10.4:

*“Investments in debt securities treated as regulatory capital by the issuer’s primary regulatory authority, and **that do not qualify** under the principles-based bond definition solely because interest can be cancelled in the event of financial stress in a non-resolution scenario without triggering an act of default are capital notes and shall be captured in SSAP No. 41—Surplus Notes. These capital notes are often issued by domestic or foreign banks, and the domestic or foreign bank regulator or the Issuer has the ability to cancel interest or dividends, without future interest accumulation or payment.”*

We are specifically concerned about the RBC treatment of certain debt instruments moving to Schedule BA for P&C/Health filers. In particular, we are focused on securities classified as “capital notes” captured in SSAP No. 41 – Surplus Notes to be reported on Schedule BA as this rule change will have unintended and uneconomic consequences for the institutions holding these highly rated instruments.

For example, a highly rated security such as the Allianz 3.2% perpetual restricted Tier 1 notes (rated A3/A by Moody’s/S&P) may classify under section 10.4 “capital notes” captured in SSAP 41 – Surplus Notes (*e.g.*, non-cumulative with optional coupon cancellation, albeit extremely remote based on issuer fundamentals and as indicated by the security ratings).

While Life insurers may be able to continue to use Filing Exempt (FE) designations or to file with the SVO to get a similar RBC factor as if it were held on Schedule D, Part 1, Bonds allowing an NAIC 1 bond factor for this instrument to be maintained on Schedule BA, P&C and Health cannot. As a result of this asset moving from Schedule D to Schedule BA, the RBC factor would increase to ~20% for P&C and Health from 1.5% and 1.9%, respectively today.

In our opinion, this reclassification imposes onerous capital requirements on a highly rated instrument (ratings which incorporate both credit and structure). We believe this deviates from the underlying fundamental risk as capital requirements would be higher than those for common equity holdings and could misallocate otherwise sound investments.

As such, we request that this matter be reviewed, and that P&C and Health insurers be able to file with the SVO/use Filing Exempt (FE) designations for RBC for capital notes reported on Schedule BA and suggest a change to P&C/Health RBC risk factors for capital notes, in line with that afforded to Life insurers. Thank you for your consideration as it relates to this matter.

Sincerely,

Jeffrey Gass and Chad Stogel
Spectrum Asset Management, Inc.
A member of the Principal Financial Group®

CC: Julie Gann, Robin Marcotte, Jake Stultz, Jason Farr and Wil Oden

Appendix: Structural ratings differentials between various credits and the prospective P&C RBC factors

					P&C		
		Moody's	S&P	Fitch	Current RBC Factor	New RBC Factor	Change in RBC Factor
Allianz	Restricted Tier 1	A3	A	N/A	1.50	20.00	18.50
	Senior Unsecured	Aa2	AA	AA-			
	Notching	4	3				
Barclays	Contingent Convertible Sec	Ba1	BB-	BBB-	5.50	20.00	14.50
	Senior Unsecured	Baa1	BBB+	A			
	Notching	3	5	4			
HSBC	Contingent Convertible Sec	Baa3	N/A	BBB	2.50	20.00	17.50
	Senior Unsecured	A3	A-	A+			
	Notching	3		4			
NatWest Group PLC	Contingent Convertible Sec	Baa3	BB-	BBB-	2.50	20.00	17.50
	Senior Unsecured	A3	BBB+	A			
	Notching	3	5	4			
Societe Generale	Contingent Convertible Sec	Ba2	BB	BB+	6.00	20.00	14.00
	Senior Non-Preferred	Baa2	BBB	A-			
	Notching	3	3	4			
Banco Santander	Contingent Convertible Sec	Ba1	BBB-	N/A	5.50	20.00	14.50
	Senior Non-Preferred	Baa1	A-	A-			
	Notching	3	3				
JP Morgan	Preferred	Baa2	BBB-	BBB+	1.00	1.00	0.00
	Senior Unsecured	A1	A-	AA-			
	Notching	4	3	4			
Bank of America	Preferred	Baa2	BBB-	BBB+	1.00	1.00	0.00
	Senior Unsecured	A1	A-	AA-			
	Notching	4	3	4			
Truist Financial	Preferred	Baa3	BBB-	BBB-	1.00	1.00	0.00
	Senior Unsecured	Baa1	A-	A-			
	Notching	2	3	3			
CMS Energy Corp	Preferred	Ba1	BBB-	BB+	2.00	2.00	0.00
	Senior Unsecured	Baa2	BBB	BBB			
	Notching	2	1	2			
Edison International	Preferred	Ba1	BB+	BB+	2.00	2.00	0.00
	Senior Unsecured	Baa2	BBB-	BBB			
	Notching	2	1	2			
Edison International	Junior Subordinated	Baa3	BB+	BB+	5.50	5.50	0.00
	Senior Unsecured	Baa2	BBB-	BBB			
	Notching	1	1	2			
NextEra	Junior Subordinated	Baa2	BBB	BBB	2.10	2.10	0.00
	Senior Unsecured	Baa1	BBB+	A-			
	Notching	1	1	2			
Prudential Fin	Junior Subordinated	Baa1	BBB+	BBB	1.80	1.80	0.00
	Senior Unsecured	A3	A	A-			
	Notching	1	2	2			

Observations:

- **NRSROs** (Nationally Recognized Statistical Rating Organizations) generally account for structural subordination in their security ratings. The greater the structural subordination, the greater the ratings notching which is reflected in the security ratings.
 - **Contingent Convertible Securities (CoCos):** For UK banks, CoCos are typically notched 3, 5, and 4 ratings lower by Moody's, S&P, and Fitch, respectively, from their senior unsecured ratings. For EU banks, CoCos are usually notched 3, 3, and 4 lower from their senior non-preferred ratings.
 - **US G-SIB preferred securities:** These are generally notched 4, 3, and 4 ratings lower from their senior unsecured ratings, while non-G-SIB bank preferreds are notched 2, 3, and 3 (or 4) lower.
 - **Junior Subordinated Securities:** These are typically notched 1, 1, and 2 ratings lower from their respective senior ratings.
- RBC factors for most securities previously classified as "hybrids" are expected to remain unchanged, except for the securities captured by section 10.4 in the "Implementation Questions and Answers" document above. Using the securities above, on average, the securities captured by 10.4 move from a ~ 4% RBC factor to 20% for P&C Insurers ~ a move of 16%.