

Date: 2/4/25

*Virtual Meeting*

**RISK-BASED CAPITAL INVESTMENT RISK AND EVALUATION (E) WORKING GROUP**

Tuesday, February 11, 2025

11:00 a.m. – 12:00 p.m. ET / 10:00 – 11:00 a.m. CT / 9:00 – 10:00 a.m. MT / 8:00 – 9:00 a.m. PT

**ROLL CALL**

Philip Barlow, Chair	District of Columbia	William Leung/ Danielle Smith	Missouri
Thomas Reedy, Vice Chair	California	Tadd Wegner	Nebraska
Wanchin Chou	Connecticut	Jennifer Li	New Hampshire
Ray Spudeck/Carolyn Morgan	Florida	Bob Kasinow/William B. Carmello	New York
Matt Cheung	Illinois	Dale Bruggeman/Tom Botsko	Ohio
Roy Eft	Indiana	Rachel Hemphill	Texas
Carrie Mears/Kevin Clark	Iowa	Doug Stolte	Virginia
Fred Andersen	Minnesota	Steve Drutz/Katy Bardsley	Washington
		Amy Malm	Wisconsin

NAIC Support Staff: Julie Gann/Maggie Chang

**AGENDA**

1. Hear an Update from the American Academy of Actuaries (Academy) on the Structured Securities Risk-Based Capital (RBC) Project —*Philip Barlow (DC)* Attachment One
2. Discuss the Status of the Fund Review Project and Consider Exposure of the American Council of Life Insurers’ (ACLI’s) RBC Principles for Bond Funds Presentation and the NAIC’s Memorandum of Bond Funds Reported in 2023 Annual Statement Filings—*Philip Barlow (DC)* Attachment Two  
Attachment Three
3. Discuss Any Other Matters Brought Before the Working Group —*Philip Barlow (DC)*
4. Adjournment

# CLO C-1 Update to Risk-Based Capital Investment Risk and Evaluation (E) Working Group (RBCIRE)

February 11, 2025

Steve Smith, MAAA, FSA, CFA  
Chairperson, Academy C-1 Subcommittee

## About the Academy

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The American Academy of Actuaries is a 20,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. For 60 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

For more information, please visit:

[actuary.org](https://www.actuary.org)

## Key Work Completed so Far

- 2022: [CLO overview](#)
- 2023: [ABS RBC principles](#)
- 2024–2025:
  - Acquisition of Moody’s CLO data
  - Collateral modeling approach
  - Scenario compression approach

## Completed: Acquisition of Moody's CLO Data

- Candidate comparable attributes
- Tranche-level data
- Deal-level data
- Collateral details
- Examples:
  - Tranche/collateral ratings (by CRP)
  - Overcollateralization
  - Tranche thickness

## Completed: Collateral Modeling Approach

- Prioritized consistency with C-1 bond factors
- Used C-1 bond model to produce loss distribution
- Adjusted for seniority of loans vs. bonds and any other known, relevant differences
- Considered closed-form approximation of loss distribution
- Stressed the timing of losses

## Completed: Scenario Compression Approach

- Could not feasibly run thousands of collateral loss scenarios through CLO cash flow model
- Could not use only a single scenario due to the cliff-shaped loss distribution of CLOs
- Instead, we will subdivide the tail of the collateral loss distribution into several discrete ranges, where the average loss of each range is run through the CLO cash flow model

## Current/Remaining Work

- Acquisition of C-1 bond factor model or results, allowing for:
  - Collateral modeling specification/approximation
  - Scenario compression specification
- Parameterization of CLO cash flow model
- Conversion of CLO cash flows into losses for C-1 capital, allowing for:
  - Identification of comparable attributes
  - Development of base factors
- Diversification & concentration



## Questions

Contact:

Amanda Barry-Moilanen, Life Policy Project Manager  
[barrymoilanen@actuary.org](mailto:barrymoilanen@actuary.org)



# RBC Principles for Bond Funds

December 2024

# Background

- Operating under a regulatory regime where funds with slightly different structures but same economic risks receive different RBC treatment
- (9/27/2017) VOSTF directed NAIC staff to develop a comprehensive proposal to ensure consistent treatment for investments that involved funds that invest in bond portfolios (history included in Appendix)
- (5/10/2019) VOSTF requested that CATF consider formally integrating the comprehensive instructions for mutual funds recently adopted for the P&P Manual into the NAIC RBC framework
- ACLI has agreed with RBC IRE to begin looking at three types of bond funds that get different treatment in RBC calculation. ACLI has been looking at these to determine whether the risk profiles are similar or different to warrant different treatment for different types of bond funds. While this work focuses on these three types of bond funds, ACLI is identifying principles that can be used to expand treatment from these types of bond funds to other similar bond fund types.

# Focus on Bond Funds – Current State

	Bond Exchange Traded Funds (ETF) <sup>1</sup>	SEC Registered Bond Mutual Funds	Private Bond Funds <sup>1</sup>
Description	Portfolios of bonds held in a 1940 Act fund structure whose ownership interests trade on a centralized securities exchange	Open-end investment company registered with the SEC under 1940 Act that invests in a portfolio of bonds but does not trade on an exchange	Fund in LLC/LP form investing in bonds for benefit of investors
Accounting Standard	SSAP 26	SSAP 30	SSAP 48
Accounting Methodology	Fair Value unless Systematic Value elected	Fair Value	Equity Method Value of Accounting
RBC Charge	Bond RBC	Equity RBC	Bond RBC
RBC Charge Methodology	SVO WARF	30% equity charge (can file and SVO can apply WARF but cannot be used for RBC)	SVO WARF
RBC Asset Concentration Factors	Excluded <sup>2</sup>	Excluded <sup>2</sup>	Look through for inclusion
SIRI <sup>3</sup> Top 10 Exposure Disclosure	Excluded <sup>2</sup>	Excluded <sup>2</sup>	Look through for inclusion
Reporting Schedule	Schedule D-1	Schedule D-2-2	Schedule BA
AVR Treatment for Realized Capital Gains/Losses	Depends on NAIC rating changes	Entirely	Entirely

<sup>1</sup> For funds meeting SVO criteria

<sup>2</sup> For funds that are diversified within the meaning of the Investment Company Act of 1940 [Section 5(b)(1)]

<sup>3</sup> Supplementary Investment Risks Interrogatories

# Focus on Bond Funds – Future State after Applying Principles

	Bond Exchange Traded Funds (ETF) <sup>1</sup>	SEC Registered Bond Mutual Funds	Private Bond Funds <sup>1</sup>
Description	Portfolios of bonds held in a 1940 Act fund structure whose ownership interests trade on a centralized securities exchange	Open-end investment company registered with the SEC under 1940 Act that invests in a portfolio of bonds but does not trade on an exchange	Fund in LLC/LP form investing in bonds for benefit of investors
Accounting Standard	SSAP 26	SSAP 30	SSAP 48
Accounting Methodology	Fair Value unless Systematic Value elected	Fair Value	Equity Method Value of Accounting
RBC Charge	Bond RBC	<b>Bond RBC</b>	Bond RBC
RBC Charge Methodology	SVO WARF	<b>SVO WARF</b>	SVO WARF
RBC Asset Concentration Factors	Excluded <sup>2</sup>	Excluded <sup>2</sup>	Look through for inclusion
SIRI <sup>3</sup> Top 10 Exposure Disclosure	Excluded <sup>2</sup>	Excluded <sup>2</sup>	Look through for inclusion
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<sup>3</sup> Supplementary Investment Risks Interrogatories

# Assumptions / Constraints for Principles

- Develop principles for consistent RBC treatment for Bond ETFs, Bond Mutual Funds, and Bond Private Funds that bear substantially the same economic risks regardless of legal form.
- The accounting for the aforementioned Bond Funds will/should not be changed because each different fund type is governed by different SSAPs.

# Application of Principles

- Candidate principles developed to evaluate and ensure consistent RBC treatment between various fund types where the underlying holdings are bonds and currently meet the criteria for the SVO WARF methodology.
- Candidate principles could be applied for substantially similar bond fund investments to Bond ETFs, Bond Mutual Funds, and Bond Private Funds (currently meet the criteria for SVO WARF methodology) that the SVO could also apply their WARF as they become known.
- Candidate principles are intended to focus on the C-1 factor exclusively (i.e., excludes concentration factors).
- Principles could be leveraged for addressing similar situations where industry or regulators note similar significantly inconsistent RBC treatment for substantially similar investments. While the principles can potentially be leveraged, they will need to be tailored, as other fund types are likely not subject to the SVO WARF methodology.

# Candidate Principles

1. Meets qualifications for SVO to apply WARF methodology
2. RBC is based on underlying economic risk
  - Regardless of accounting method applied, fund risk depends on the collateral pool
  - Differences between fund types are considered immaterial where such differences are deemed not to contribute risks captured by RBC (e.g., illiquidity is not measured by C-1)
3. Economic risk of fund investment is materially similar to the collateral pool
  - There are no support tranches
  - All fund investors have equal ownership status (i.e., no fund investors are more senior nor junior than others)
4. Included within an SSAP in AP&P Manual



# Focus on Bond Funds – Future State after Applying Principles

	Bond Exchange Traded Funds (ETF) <sup>1</sup>	SEC Registered Bond Mutual Funds	Private Bond Funds <sup>1</sup>
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<sup>3</sup> Supplementary Investment Risks Interrogatories

# Key Questions for Regulators

- Which candidate-principles do regulators support?
- Are there additional principles not outlined herein that also ought to be incorporated into RBC for funds?

# Appendix: History of VOSTF Treatment of Funds Investing in Bonds

- 1991 – Money market mutual funds that hold short-term U.S. Treasuries - exempted from reserve
- 1992 – Funds holding U.S. direct and full faith and credit obligations - exempted from reserving
- 1992 – Funds holding high quality corporate bonds & U.S. Government obligations - reserve as NAIC 1 bonds
- 1995 – Short-term bond funds - holding high quality corporate & U.S./GSO obligations) - Schedule D; market value & reserved as bonds for AVR and RBC
- 2003 – Exchange Traded Funds that held bonds – report as bonds
- 2005 – BA assets with fixed income characteristics can be assigned NAIC Designations
- 2017 – SVO authorized to assign NAIC Designations to private Schedule BA funds, joint ventures or partnership interests if underlying investments are fixed-income like to align with Annual Reporting Instruction

**MEMORANDUM**

TO: Risk-Based Capital Investment Risk and Evaluation (E) Working Group members and interested parties  
 FROM: Philip Barlow, Chair of the Risk-Based Capital Investment Risk and Evaluation (E) Working Group  
 DATE: January 6, 2025  
 RE: Certain Bond funds reported in 2023 Annual Statement Filings

**Background**

On October 22, 2024, the Working Group met and discussed the status of the Working Agenda #2 & #4 (collectively the “Fund Review Project”). Representatives from the American Council of Life Insurers (ACLI) proposed, and the Working Group agreed, to narrow the scope of the project with the intent to achieve convergence in RBC treatment among three types of funds when they predominantly invest in bonds and receive SVO-assigned designations: 1) exchange-traded funds (ETFs), 2) U.S. Securities and Exchange Commission (SEC)-registered mutual funds; and 3) private funds.

NAIC staff was directed to summarize herein the amount of respective fund types reported on insurers’ 2023 annual statement filings to facilitate the Working Group’s discussions.

	<b>Bond Exchange Traded Fund (SVO-identified)</b>	<b>SEC Registered Bond Mutual Funds (SVO-identified)</b>	<b>Private Bond Funds (SVO-identified)</b>	<b>Total Invested Assets</b>
	Schedule D – part 1 Bonds Line 1619999999	Schedule D – part 2 – Section 2 Common Stock Line 5319999999, 5519999999, 5719999999	Schedule BA, Part 1, Line 0799999999, 0899999999, 1399999999, 1499999999, 159999999999, 169999999999 <sup>Note A</sup>	2023 Asset Page Line 12
	<b>(as % of Total Invested Assets)</b>	<b>(as % of Total Invested Assets)</b>	<b>(as % of Total Invested Assets)</b>	
<b>2023 Life</b>	\$5,844,611,923 <b>(0.11%)</b>	\$95,524,695 <b>(0.00%)</b>	\$5,858,319,676 <b>(0.11%)</b>	\$5,470,188,985,349
<b>2023 P/C</b>	\$4,934,503,172 <b>(0.19%)</b>	\$1,652,371,654 <b>(0.06%)</b>	\$905,395,147 <b>(0.03%)</b>	\$ 2,662,293,397,830
<b>2023 Health</b>	\$1,292,501,879 <b>(0.36%)</b>	\$877,352,361 <b>(0.24%)</b>	\$118,990,522 <b>(0.03%)</b>	\$360,699,408,453

**Note A**, per 2023 AVR instruction, “... the book/adjusted carrying value of all Schedule BA assets owned where the characteristics of the underlying investment are similar to bonds (Lines 07999999 and 08999999 **and the portion of Lines 13999999, 14999999, 15999999 and 16999999 that applies to fixed income instruments similar to bonds**) that have been valued according to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* ...” should be reported on Line 22 through 28 of AVR Equity Component table, thereby afforded RBC charge based on NAIC Designation. As there is no AVR reporting for P/C and Health, the statistics are obtained directly from lines 07999999, 08999999, 13999999, 14999999, 15999999, and 16999999 of Schedule BA, Part 1. As such, overstatement is expected.

Please contact NAIC Staff of Risk-Based Capital Investment Risk and Evaluation (E) Working Group with any questions.

Cc: Julie Gann, Maggie Chang, Eva Yeung, Kazeem Okosun, Derek Noe