

MEMORANDUM

TO: Tom Botsko, Chair Representative of the Capital Adequacy (E) Task Force and Chair of the Property and Casualty Risk-Based Capital (E) Working Group and
Steve Drutz, Chair of the Health Risk-Based Capital (E) Working Group
Philip Barlow, Chair of the Life Risk-Based Capital (E) Working Group and Chair of the Risk-Based Capital Investment Risk and Evaluation (E) Working Group
Pat Gosselin, Chair of the Blanks (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: January 23, 2024

RE: Collateral Loan Reporting Changes

At the 2023 Fall National Meeting, the Statutory Accounting Principles (E) Working Group exposed agenda item *2023-28: Collateral Loan Reporting*, which proposes to expand Schedule BA Collateral Loans disclosures and reporting lines to quickly identify the type of collateral in support of admittance of collateral loans in scope of *SSAP No. 21R—Other Admitted Assets*. Currently, collateral loans are only divided by affiliated or unaffiliated and do not identify the various investment categories of underlying collateral. There are also proposed new disclosures to aggregate and identify what is admitted and not admitted within each of those newly proposed investment categories.

Since the existing Schedule BA Collateral Loans reporting lines have a connection to the Asset Valuation Reserve (AVR) and/or Risk Based Capital (RBC) schedules and instructions, we recognize the potential for corresponding revisions to them, and ask for your input. As discussions take place, we will keep you notified of significant changes that occur; and after completion we will forward referrals as necessary. For reporting changes, SAPWG typically sponsors Blanks changes to the Annual Statements, which would include necessary changes in format/instruction to the AVR schedule for the Life statement. We expect the format of RBC schedules and related instructional changes will happen within the RBC working groups in due course, as well as any consideration of risk charges for the proposed expansion lines based on underlying collateral. Please note that the AVR schedule and Life RBC schedules work together and may require some planning on all groups' parts. We also wanted to make you aware that during discussions of reporting changes under the bond project, we identified that some companies are reporting collateral loans as non-private equity funds, which then obtain RBC charges based on the underlying collateral assets.

The agenda item is initially exposed until Jan. 22, 2024, and includes a direct request to industry to provide comments on the proposed collateral loan reporting lines. NAIC staff expects further discussion on the extent of reporting lines needed and how those lines should be mapped to AVR for life companies.

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If you have any questions, or would like to further discuss, please contact the Statutory Accounting Principles (E) Working Group chair or vice chair (Dale Bruggeman, or Kevin Clark), or NAIC staff Julie Gann (jgann@naic.org).

Cc: Julie Gann, Robin Marcotte, Jake Stultz, Jason Farr, Wil Oden, Mary Caswell, Crystal Brown, Dave Fleming, Eva Yeung, Maggie Chang

MEMORANDUM

TO: Philip Barlow, Chair of the Life 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: February 29, 2024
RE: Collateral Loan Reporting Changes – SAPWG Actions Feb. 20, 2024

On Feb. 20, 2024, the Statutory Accounting Principles (E) Working Group (SAPWG) considered agenda item 2023-28: *Collateral Loan Reporting*, which proposed to expand collateral loan disclosures and Schedule BA reporting lines in accordance with the type of collateral supporting the collateral loan pursuant to SSAP No. 21R—*Other Admitted Assets*. During this call the Working Group took the following actions:

- 1) Adopted a new disclosure to detail the collateral loans admitted and nonadmitted by type of underlying collateral. This disclosure is required for year-end 2024 and a blanks proposal is being sponsored to facilitate data capturing for 2024 reporting.
- 2) Exposed revised Schedule BA reporting lines to require allocation of collateral loans based on the underlying collateral. With this exposure, the Working Group specifically requested comments from regulators and industry on whether collateral loans backed by certain types of collateral should flow through the Asset Valuation Reserve (AVR) for risk-based capital (RBC) impact. With this request, a referral was directed to the Life Risk-Based Capital (E) Working Group (LRBCWG) to request feedback on the proposed reporting lines and the potential to map certain collateral loans to AVR for RBC purposes.

With the discussion that occurred on Feb. 20, 2024, it was identified that collateral loans do not currently flow through AVR. From historical review, the exclusion from AVR has been attributed to a 1990 intercompany survey where it was identified that collateral loans were very small risks and a small proportion of total portfolio value. Collateral loans were originally captured on Schedule C, and when that schedule was eliminated and the reporting moved to Schedule BA, a change to flow through AVR was not incorporated. Currently all investments reported as collateral loans, regardless of the underlying collateral that supports the loan, receive the same 0.0680 life RBC factor charge.

It has been identified that some reporting entities are currently reporting certain collateral loans in the Schedule BA “non-registered private fund” reporting category allocated by underlying collateral so that they flow through AVR for RBC impact. The discussion on Feb. 20, 2024, noted that this reporting causes consistency concerns, and the regulator’s need for comparable financial information is paramount in determining an insurer’s financial condition.

To improve overall reporting, the SAPWG is sponsoring blanks changes to eliminate and clarify the purpose of certain reporting lines on Schedule BA. These changes include eliminating the “non-registered private fund” category and clarifying that such funds shall be reported in the “joint ventures, partnerships, or limited liability companies” reporting category. The sponsored blanks revisions further clarify the types of investments permitted for reporting in certain categories with inclusion of an explicit statement that investments shall be reported in the appropriate dedicated reporting line, and if such a line does not exist for a specific investment, it shall be reported as an “Any Other Asset.” These changes are captured in the Blanks (E) Working Group proposal 2023-12BWG that also details the new reporting lines for the non-bond debt securities in response to the bond project. This proposal is exposed for comment until April 23, 2024.

Although efforts to improve consistent reporting are underway, with the overall increase in collateral loans and actions by industry to report certain loans in categories that flow through AVR to reflect the underlying asset risk, this referral requests feedback from the LRBCWG on the allocation of collateral loans through AVR. Key elements to highlight for LRBCWG potential consideration include:

- An approach that maps reporting of certain collateral loans through existing AVR categories may not necessitate extensive RBC changes. Rather, specific reporting lines would map through the blanks reporting process to the identified AVR category and flow through automatically to the RBC schedule. If this approach is taken, the RBC revisions could potentially be limited to clarifying the items that continue to flow through to the existing collateral loan line.
- If an approach to map certain collateral loans through existing AVR categories is supported, information is requested on which collateral loans should be given this treatment. For example, information received from industry has indicated that “warehouse loans¹” with mortgage loan collateral have been reported as “non-registered private funds” with underlying characteristics of mortgage loans. This reporting facilitates a “look-through” RBC treatment whereby the mortgage RBC criteria is applied to the mortgage loans underlying the warehouse loan. Although this reporting has likely resulted in a more desirable RBC impact than the collateral loan classification, industry has continued to report loans backed by LLC interests as collateral in the collateral loan category, where look-through treatment would be less favorable. By reporting these items as collateral loans, the RBC factor was 0.0680 in comparison to a 0.3000 charge that could occur² if reported based on the underlying collateral. Ultimately, feedback is requested on whether loans backed by certain types of collateral should be treated differently through AVR as well as comments on when loans backed by certain types of collateral should be treated differently than other collateral loans.
- The existing collateral loan RBC factor is believed to have been established without much analysis, but rather reflects a blended rate of RBC charges. This was likely supported due to the historical small risk and population of collateral loans. From assessments of 2022 data, collateral loans make up a significant portion of assets at some companies, and it is anticipated that a significant number of collateral loans are backed by LLC interests. Unfortunately, underlying collateral data is limited to what is discernable from a review of the description captured in Schedule BA and only captures what was reported as collateral loans and not within another reporting category. The Working Group’s adoption of a new 2024 disclosure and reporting clarifications shall assist in providing improved information on the population of collateral loans,

¹ For reference, a “warehouse loan” is a loan to an originator of financing products (e.g. mortgage loans, consumer loans, middle market corporate loans, etc.) that is secured by the assets being originated. It is a temporary form of financing often used to “warehouse” the underlying collateral until sufficient scale is achieved to allow the collateral to be securitized.

² It is worth noting that there would typically be some level of overcollateralization when comparing the amount of loan and the underlying value of the LLC collateral.

and the underlying collateral that backs loans if the LRBCWG believes it is appropriate to complete a more detailed analysis of this asset category for RBC purposes.

Consistent with the prior referral dated Jan. 17, 2024, the SAPWG will continue to keep the LRBCWG informed of the discussions involving collateral loans. The proposed reporting lines for collateral loans are exposed at SAPWG until April 19, 2024, and are detailed within. As noted, this exposure specifically requests comments on whether collateral loans backed by certain types of collateral should flow differently through AVR for RBC impact. The SAPWG will share information received from this exposure with the LRBCWG to assist with further discussion, but also welcomes initial responses from the LRBCWG on this inquiry as well as the proposed reporting lines.

If you have any questions, or would like to further discuss, please contact the Statutory Accounting Principles (E) Working Group chair or vice chair (Dale Bruggeman, or Kevin Clark), or NAIC staff Julie Gann (jgann@naic.org).

February 20, 2024, SAPWG Exposed Schedule BA Collateral Loan Reporting Changes:

Collateral Loans – Reported by Qualifying Investment Collateral that Secures the Loan

Bonds and Asset-Backed Securities (SSAP No. 26R & SSAP No. 43R)

Unaffiliated.....
Affiliated.....

Preferred Stocks (SSAP No. 32R)

Unaffiliated.....
Affiliated.....

Common Stocks (SSAP No. 30R)

Unaffiliated.....
Affiliated.....

Mortgage Loans (SSAP No. 37R)

Unaffiliated.....
Affiliated.....

Real Estate (SSAP No. 40R)

Unaffiliated.....
Affiliated.....

Joint Venture, Partnerships or Limited Liability Companies (SSAP No. 48)

Fixed Income Investments (Unaffiliated)
Fixed Income Investments (Affiliated)

Common Stocks (Unaffiliated)
Common Stocks (Affiliated)

Real Estate (Unaffiliated)
Real Estate (Affiliated)

Mortgage Loans (Unaffiliated)
Mortgage Loans (Affiliated)

Other (Unaffiliated)
Other (Affiliated)

Other Investment Category

Cash, Cash Equivalent and Short-Term Investments (Unaffiliated)
Cash, Cash Equivalent and Short-Term Investments (Affiliated)

Other Long-Term Invested Assets (Unaffiliated)
Other Long-Term Invested Assets (Affiliated)

Non-Collateral Loans

Related Party / Affiliated Loans.....
All Other Non-Collateral Loans.....

Cc: Julie Gann, Robin Marcotte, Jake Stultz, Jason Farr, Wil Oden, Crystal Brown, Dave Fleming, Eva Yeung, Maggie Chang