A reminder of current initiatives

Several significant long-term initiatives that regulators have prioritized:

- **Life RBC**
  - RBC Covariance (possibly related to the portfolio adjustment function (PAF)/size factor)
  - Structured Securities Project (with the Academy) (possibly related to the PAF/size factor)
    - Refinements to the CLO RBC C-1 factors, including possible differentiation of MM CLOs
  - RBC C-3 Harmonization & GOES (with the Academy and Conning)
  - Longevity risk (with LATF)
- **Property & Casualty RBC**
  - Climate-related catastrophe risks, including severe convective storms (SCS) and broader climate hazards.
  - R-4 (Reserve Risk) & R-5 (Premium Risk) Loss/Premium Concentration Factors
- **Health RBC**
  - H-2 Underwriting risk charge (with the Academy), managed care credit
  - Stop loss assessment
  - Long-term care assessment

RBC Component (in no particular order)	Description	Materiality benchmark (2025)	Effort
Life reinsurance transactions	While RBC includes a reserve credit and recoverables charge, they are coarse. In addition, the use of arrangements in non-Reciprocal jurisdictions has grown. Thus, the need to assess risks and RBC treatment.	Reserve credit and ModCo has reached ~$2.85 trillion, with ~$135 billion for non-Reciprocal jurisdictions.	Significant
P&C reinsurance transactions	While RBC includes counterparty recoverables charge, by credit quality and collateral, arrangements in non-Reciprocal jurisdictions and nontraditional reinsurance have grown. Thus, the need to assess risks and RBC treatment.	Ceded reserves to non-Reciprocal jurisdictions reached $42 billion in 2025.	Significant
Life residential mortgage loans	Residential mortgages can range from a few hundred thousand to a several hundred million dollar townhouse development that can face significant differences in their risk characteristics. An assessment of whether the current 68 bps charge (~A-rated corporate bond), which was not empirical-based, accurately reflects the risks is needed.	Residential mortgages reached ~$150 billion, exhibiting significant growth, over 30% in 2025. In 2018, holdings were $18 billion.	Moderate
RMBS and CMBS	1. RMBS & CMBS Intrinsic Price (IP) Designations have characteristics that deviate significantly from agency ratings, including having a maturity effect. 2. An assessment of whether corporate C-1 bond factors are appropriate for Life RMBS and CMBS RBC is needed, with considerations for their unique structural features.	1. IP Designations are estimated to result in A2-rated 5-year tranche receiving over 40 times the capital of A2-rated 1-year tranche. 2. CMBS at $148 billion and RMBS at $133 billion ($9^{th}$- and 10^{th}-life asset classes)	1. Moderate 2. Significant
Life RBC Covariance, including the treatment across asset classes, and the portfolio adjustment factor	Life RBC Covariance assumptions are coarse, generally set at 100% or 0%, which clearly don't reflect reality. Furthermore, the current simplistic structure does not lend itself to recognizing diversification or concentration risks across the broad set of assets that face disparate risks (e.g., corporate, municipal, and consumer backed securitizations). An assessment of the RBC Covariance structure (e.g., cross asset class) and parameters is needed.	A hypothetical insurer with 3% of its portfolio invested in common stock would have its RBC drop from 446% to 384% if, say, common stock-bond correlations of 50% were used, as is the case with Solvency II.	Significant

RBC component (in no particular order)	Description	Materiality benchmark (20025)	Effort
P&C Rcat correlation	Correlations among hurricane, wildfire, and severe convective storm risks to be assessed and update the Rcat calculation formula accordingly.	SCS exposures have grown materially, from $19 billion in 2019 to $47 billion in 2024.	Significant
H-2 Underwriting Risk	Underwriting risk factors need to be assessed and updated, including diversification credit, stop-loss, LTC, and managed care credit.	Direct incurred claims + change in contract reserves = $1.278 trillion • Stop-loss = $34.2 billion • LTC = $23.3 billion • Managed care credit proxy = $1.03 trillion	Significant
Life principle-based capital (RBC C-3)	While the current focus on revising C-3 has been on fixed and variable annuities, and life products that are single-premium, there hasn't been a recent significant effort to align RBC C-3 calibration for life products that are not single-premium. Life recurring-premium and other products are subject to static factors, which should be modernized and principle-based.	At well over $1 trillion, non-single-premium life policies are significant, constituting most life policies. C-3 constitutes roughly 6.5% of Life RBC.	Significant
Life RBC factor-Designation grid mismatch	Schedule D-1 bonds use the granular 20-class C-1 grid. Schedule BA fixed-income is charged the *coarse pre-2021 6-class* grid and the 2021 PAF, which should be assessed for possible update.	Most Schedule BA Designations 1 ($27 billion) and 2 ($11 billion) receive a lower RBC charge, which can be less than 50% if reported on Schedule D-1.	Moderate
Life investment valuation-basis mismatch	Applying bond and mortgage factors to Schedule BA debt may not be appropriate, which needs reviewing, given mismatched valuation. For example, Schedule B mortgages, generally measured at amortized cost, while Schedule BA funds are measured under U.S. GAAP equity method.	The carrying value of Schedule BA commercial mortgages, for example, is $32 billion, 32% of which are valued below cost, with an average markdown of -20%.	Moderate

Gaps & inconsistencies: Model governance

While detailed direction has not been provided on model governance, the proposed process for identifying and prioritizing gaps & inconsistencies does follow the spirit of the formative *RBC Model Risk Management Guidelines* that Bridgeway compiled and reviewed with industry stakeholders.

The Drafting Group acknowledged the benefits of formalizing coordination across the various Task Forces and Working Groups.

The Drafting Group explored questions related to governance in almost every session, keeping in mind notable points from commenters:

- The question of how RBC charges are set and whether there is a better assignment – examples that were discussed:
  - Life investment valuation-basis mismatch that was included on the list, where, for example, CM factors from Schedule B are applied to Schedule BA mortgage funds.
  - 'Other' categories may be too broad, such as JV, LLC, LP – Other, or Other Financial-Backed ABS Self-Liquid with Other Collateral ($41 and $125 billion life holdings in 2025, respectively), given the differentiated risks.
- Whether the prioritization process is sound, and whether a more formal process is needed for new asset classes to receive dedicated capital charges?
- What process should be followed when assessing whether RBC charges need re-evaluation?

Additional discussion is needed to assess how the processes should be structured.

Areas warranting further study

1. **Operational risk charge**. The operational charge (3% x RBC before the operational charge) is not based on an empirical study. The Drafting Group agreed that both qualitative and quantitative assessments of the risks were needed and that the concept needed to be better defined. However, the Drafting Group acknowledged significant challenges, including a possible costly data collection effort. While it was worth conducting a literature review to assess whether there are recent studies on the matter, the Drafting Group concluded the risk was not obviously material. 2025 RBC operational risk totals: (a) ~$0.6 billion (net of C-4a) for Life RBC, (b) ~$14 billion for P&C RBC, and (c) ~$2.7 billion for Health RBC. The effort is expected to be significant.

2. **RBC outliers**. An analysis of companies with high RBC ratios, breaking down how they allocate total available capital and the authorized control-level RBC, could identify some RBC gaps. The effort is expected to be moderate.

Items the Drafting Group did not prioritize at this time (1 of 2)

- **Health reinsurance.** The Drafting Group did not view health reinsurance as a material or emerging risk, although recent growth suggests it warrants monitoring. In 2025, incurred claims + change in contract reserves = $1.3 trillion, with reinsurance recoverables at under $30 billion.
- **Limitations with the Health RBC formula**. RRC's comment letter included several limitations with the Health RBC formula (Attachment Three). While the Drafting Group did not disagree with the list, there was no accompanying assessment of materiality, nor was there an immediate way for the Drafting Group to assess materiality. As with other items, stakeholders advocating for prioritizing updates to the RBC formula should provide a materiality assessment.
- **Significant variation in the calibration of Life RBC investment components**. Athene's comment letter (Attachment Three) highlighted significant variation in model calibration across bonds, commercial mortgages, residential mortgages, real estate, common stock, and other asset classes, including the risk horizon, statistical safety level, Statutory Accounting, discounting, reinvestment, and other modeling features. For example, commercial real estate mortgage CM factors were estimated at a 92% VaR, while the C-1 bond factors were estimated at a 96% VaR. *2021 Revisions to the RBC C-1 Bond Factors.pdf* demonstrates the difference can be significant, with C-1 VaR 96% factors ~40% – 80% higher than VaR 92%. While the Drafting Group acknowledged the variation in calibrations, regulators pointed to deliberate decisions (such as those involving different time horizons) to deviate from benchmarks (e.g., VaR 96) and noted that such deviations alone were insufficient to justify prioritizing updates to those components. As with other items, stakeholders advocating to prioritize an update to the RBC formula should provide an assessment of materiality.

Items the Drafting Group did not prioritize at this time (2 of 2)

- **Life policyholder behavior risk**. RRC advocated for the modeling of behavioral risk. While the Drafting Group did not disagree with RRC that behavior risk was important, embarking on the effort was viewed as too significant in the context of the other priorities.
- **Business practices, including concentrated investment strategies for an identifiable segment of companies**. Several business practices were identified for segments of the industry that the Drafting Group felt were better addressed elsewhere in the framework or were sufficiently narrow that they could be addressed by a state insurance department rather than by utilizing limited RBC resources.
- **P&C, Lines subject to tail risk (e.g., Personal Injury Protection or mass tort), smaller companies increased underwriting risk, and cat risk adjustment does not address all perils (e.g., Severe Convective Storms)**. RRC raised several limitations with the P&C formula, many of which the Drafting Group felt may be legitimate candidate items but required more details and an assessment of materiality.