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ASSOCIATION

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February 17, 2023

Mr. Philip Barlow, Chair
RBC Investment Risk & Evaluation (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Valuation of Securities (E) Task Force referral and risk-based capital (RBC) structural proposal addressing residual tranches

Dear Mr. Barlow

The Structured Finance Association (SFA) appreciates the opportunity to provide feedback on the referral from the Valuation of Securities (VOS) (E) Task Force (VOS TF) to the Risk Based Capital Investment and Risk Evaluation Working Group (RBCIRE WG) on the proposed interim subcategories within the current NAIC Category 6. Our members expressed an interest in providing feedback to this exposure, especially given the degree of subject matter overlap on related exposure drafts from VOS (E) TF.

The Structured Finance Association's mission is: "*To help its members and public policy markers grow credit availability and the real economy in a responsible manner*." Insurance companies actively participate in the structured finance market including as investors. As such the purpose of imposing a risk-based capital (RBC) requirement as a foundational element to ensuring that insurance companies can fulfill their financial obligations to insurance policyholders is keenly aligned with our mission.

The Structured Finance Association is a consensus-driven trade association with over 370 institutional members representing the entire value chain of the securitization market. By facilitating the responsible issuance and investing of loans and securities, the market provides trillions of dollars of capital to consumers and businesses in communities across the country. SFA members include issuers and investors, broker-dealers, rating agencies, data analytic firms, law firms, servicers, trustees and accounting firms. As such, unlike many trade associations, before we take any advocacy position our governance requires us to achieve consensus by agreement rather than majority vote, ensuing the perspective of all our diverse membership are included. This diversity is our strength, as it builds healthy tension in arriving at our consensus position. Because of this, we are methodical and thoughtful as we analyze the pros and cons of regulatory proposals before we reach a mutually acceptable position.

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Given the alignment of SFA mission with the purpose of RBC requirements, our membership quickly built full consensus in support of the RBCIRE WG's goal to eliminate any material RBC arbitrage. Our members also believe that the RBC requirements must account for the unique structures and risk profiles of bank loans versus CLOs. However, our membership is split on the interim process and approach that the RBCIRE WG has recommended to accomplish this goal. As a consequence, in this instance where there is not consensus, we will instead inform RBCIRE WG and other policymakers of the differing views. Additionally, while all members who participate in the CLO market were invited to participate in our consensus building process, below we have only highlighted the differing viewpoints of our insurance company members as they are the economic stakeholders most directly impacted by the proposed RBC levels.

Below our feedback focuses on two areas: (1) The proposed interim RBC capital levels of 30%, 75%, and 100%, and (2) The potential application of the proposed interims RBC levels.

1. ***Proposed Interim Capital Levels of 30%, 75%, and 100%***

In seeking to achieve consensus amongst our members, approximately 70% of the insurance companies believed that more work is needed prior to instituting any changes to NAIC Category 6 RBC levels even if only proposed to be interim given the lack of direct supporting analysis behind the RBC levels of 30%, 75%, and 100% within NAIC Category 6. As noted in the American Academy of Actuaries presentation, those levels are not supported by data related to the performance of the CLO tranches which would justify the creation of such levels. Given that, these insurance company members believe that the proposed interim levels should not be adopted until RBCIRE WG has performed an analysis to justify any new interim or permanent RBC levels.

On the other hand, approximately 30% of our insurance company members believe that it would be appropriate for RBCIRE WG to proceed with the proposed changes to NAIC Category Six and implement interim subcategories of 30%, 75%, and 100%. They noted that the current level of 30% is equally unsupported by any analysis and believe that the interim categories more closely reflect the relevant risk of residual tranches in NAIC Category 6. Importantly, they note that these interim factors, when used under the SVO's proposed modeling of CLOs for NAIC designation determination, will provide RBC alternatives for the SVO to select from based on which one better aligns with the actual modeling results. This process of modeling itself, these insurers argue, will provide the necessary analysis to ensure the appropriateness of whichever of the 3 interim designations is selected for a particular modeled residual tranche.

2. ***Clarification on Applicability of Category 6 Subcategories***

Nonetheless, regardless of the their viewpoint on the adoption of the proposed interim subcategories within NAIC Category 6, SFA members collectively share a call for the RBCIRE WG to clarify whether such interim RBC charges would apply only to CLOs or apply more broadly to residuals across all asset classes. The VOS (E) TF referral referenced CLOs, and presumably forms the basis for the newly proposed interim levels. However, our members expressed that it was not clear whether VOS (E) intended the referral to apply only to CLOs, or whether—if such levels were to be adopted—RBCIRE WG would intend that they apply to residuals across other structured finance asset classes as well. We therefore urge RBCIRE WG to clarify whether any changes to subcategories within NAIC Category 6 apply narrowly (i.e., only to CLOs) or broadly (i.e., across all structured securities).

Once again, we thank you for the opportunity to share our members views on these points and look forward to continuing engaging with you on these topics. If you have any questions, please do not hesitate to contact SFA staff.

Regards,

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Kristi Leo
President, Structured Finance Association