

## 2022 Proposed Charges

### FINANCIAL STABILITY (E) TASK FORCE

The mission of the Financial Stability (E) Task Force is to consider issues concerning domestic or global financial stability as they pertain to the role of state insurance regulators.

#### Ongoing Support of NAIC Program, Products or Services

1. The **Financial Stability (E) Task Force** will:

- A. Consider issues concerning domestic and global financial stability as they pertain to the role of state insurance regulators and make recommendations to the International Insurance Relations (G) Committee, the Government Relations (EX) Leadership Council and/or the Executive (EX) Committee, as appropriate.
  1. Analyze existing post-financial crisis regulatory reforms for their application in identifying macroeconomic trends, including identifying possible areas of improvement or gaps, and propose to the Financial Condition (E) Committee or other relevant committee enhancements and/or additions to further improve the ability of state insurance regulators and the industry to address macroprudential impacts; consult with such committees on implementation, as needed.
- B. Consider state insurance regulators' input to national and international discussions on macroeconomic vulnerabilities affecting the insurance sector.
  1. Monitor international macroprudential activities at forums like the International Association of Insurance Supervisors (IAIS).
  2. Implement the Macroprudential Initiative (MPI) domestically, which includes enhancements to the U.S. regulatory toolkit as part of the *State Ahead* initiative.
- C. Serve as a forum to coordinate state insurance regulators' perspectives on a wide variety of issues arising from the designation of a U.S. insurance group as "systemically important" and "internationally active" both pre- and post- designation, including:
  1. Where appropriate, develop policy recommendations and/or guidance regarding the role, responsibilities and activities of state insurance regulators in the context of consolidated supervision resulting from designation.
  2. Analyze proposed rules by the federal agencies that relate to financial stability.
  3. Analyze proposed policy measures regarding supervisory standards for global systemically important insurers (G-SIIs) and internationally active insurance groups (IAIGs).
  4. Develop comment letters on such analysis for further consideration by the International Insurance Relations (G) Committee, the Government Relations (EX) Leadership Council, and/or the Executive (EX) Committee, as appropriate.

2. The **Macroprudential (E) Working Group** will:

- A. Oversee the implementation and maintenance of the liquidity stress testing framework for 2020 data as well as future iterations.
- B. Assist with the remaining **MPI projects related to counterparty disclosures and capital stress testing** as needed.
- C. Continue to develop and administer data collection tools as needed, leveraging existing data where feasible, to provide the Financial Stability (E) Task Force with meaningful macroprudential information regarding how the insurance sector is navigating the prevailing market conditions.
- D. Oversee the development, implementation, and maintenance process for a new Macroprudential Risk Assessment system (i.e., policies, procedures, and tools) to enhance regulators' ability to monitor industry trends from a macroprudential perspective.
- E. Oversee the documentation of the NAIC's macroprudential policies, procedures, and tools.
- F. Provide the Task Force with proposed responses to IAIS and other international initiatives as needed.

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# PE Owned Insurance Companies

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NATIONAL ASSOCIATION OF  
INSURANCE COMMISSIONERS



# PE and Insurance Companies

- Private Equity (PE) firms have increasingly been intertwined with insurance companies.
  - This trend is driven by low interest rates as well by changing PE business models.
- NAIC's Capital Markets Bureau (CMB) maintains a manually researched and constantly updated list of 177 companies owned or controlled by PE.
- We have published and will continue to publish analytical research on the holdings of those companies we identify.
  - One major take-away is that PE-owned companies focus far more on investing in asset backed securities (ABS) than the industry as whole: 25% vs 10% of total bonds in 2020.

*For more information please see:*

[Private Equity \(PE\) Owned U.S. Insurers as of Year-End 2020](#)

and

[Private Equity Primer](#)



# Statement of the Concern

- Concern about PE ownership of insurance companies has been broadly expressed by regulators, staff and our federal colleagues.
- However, to be actionable, these concerns need to be translated into a specific characteristic or behavior which differentiates the PE ownership structure from other insurance companies.
- Here, we attempt to use a “first principles” approach to zero in on the concern as well as listing potential next steps.



# Affiliated Transactions

- Related party transactions have been a key area of concern for solvency oversight since historically this is where many issues arise.
  - Statutory accounting and reporting specifically address affiliated transactions.
  - Furthermore, state laws include provisions that require approval of certain (e.g., service agreements) affiliated agreements.
- Domiciliary regulators consider concerns when reviewing and approving Form A applications and those concerns are also addressed in NAIC committee groups such as FAWG.

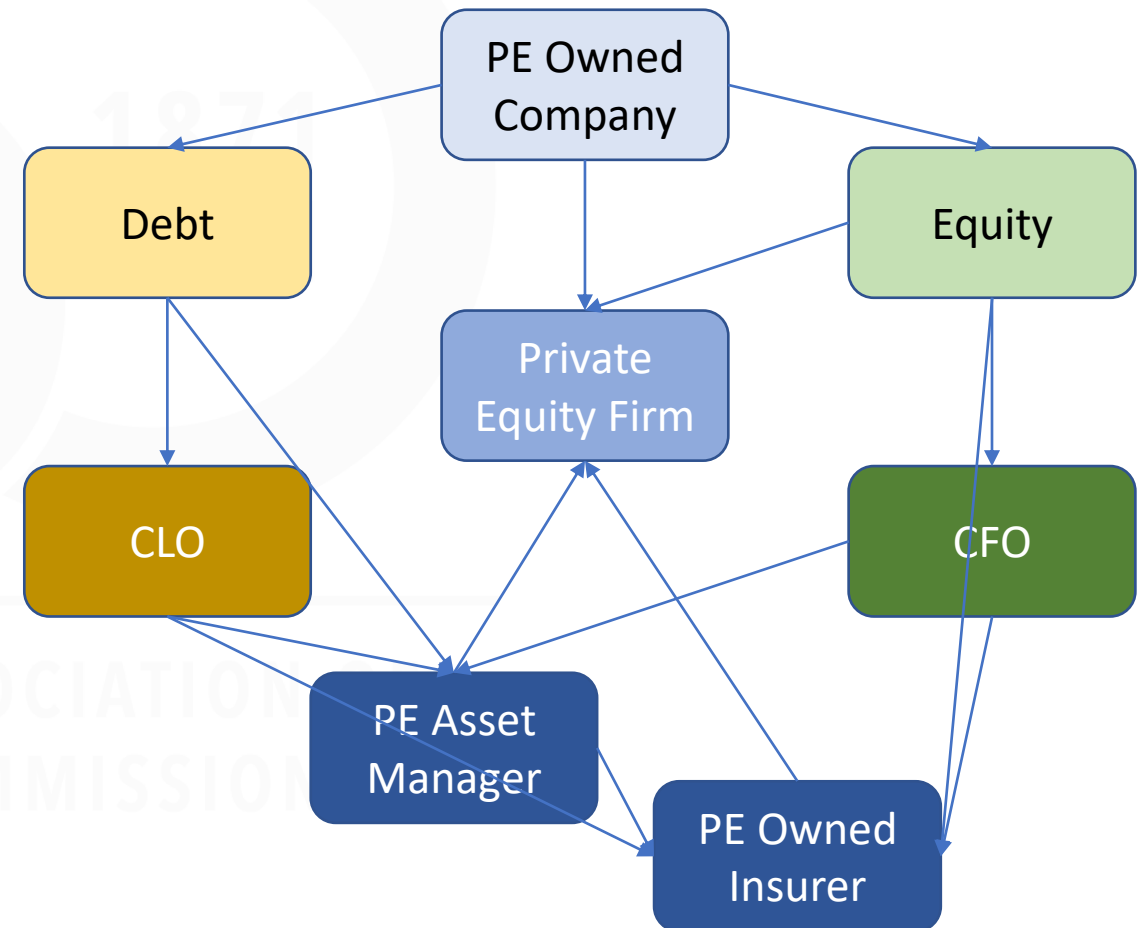


# Novel Regulatory Risks

- The current regulatory framework was developed in the context of **stock companies** and mutuals. In these companies **controlling parties use dividends and salaries / benefits to extract value for themselves, which may be excessive.** Thus, regulations focus on oversight of these channels of value extraction (i.e. gating dividends and salaries in certain cases).
- Unlike stock companies and mutuals, **PE-owned companies look to extract value via fees (not primarily dividends or salaries)**
  - **Affiliated transactions are considered by regulators, but it is not clear if all appropriate PE transactions are captured.**

# PE Business Model

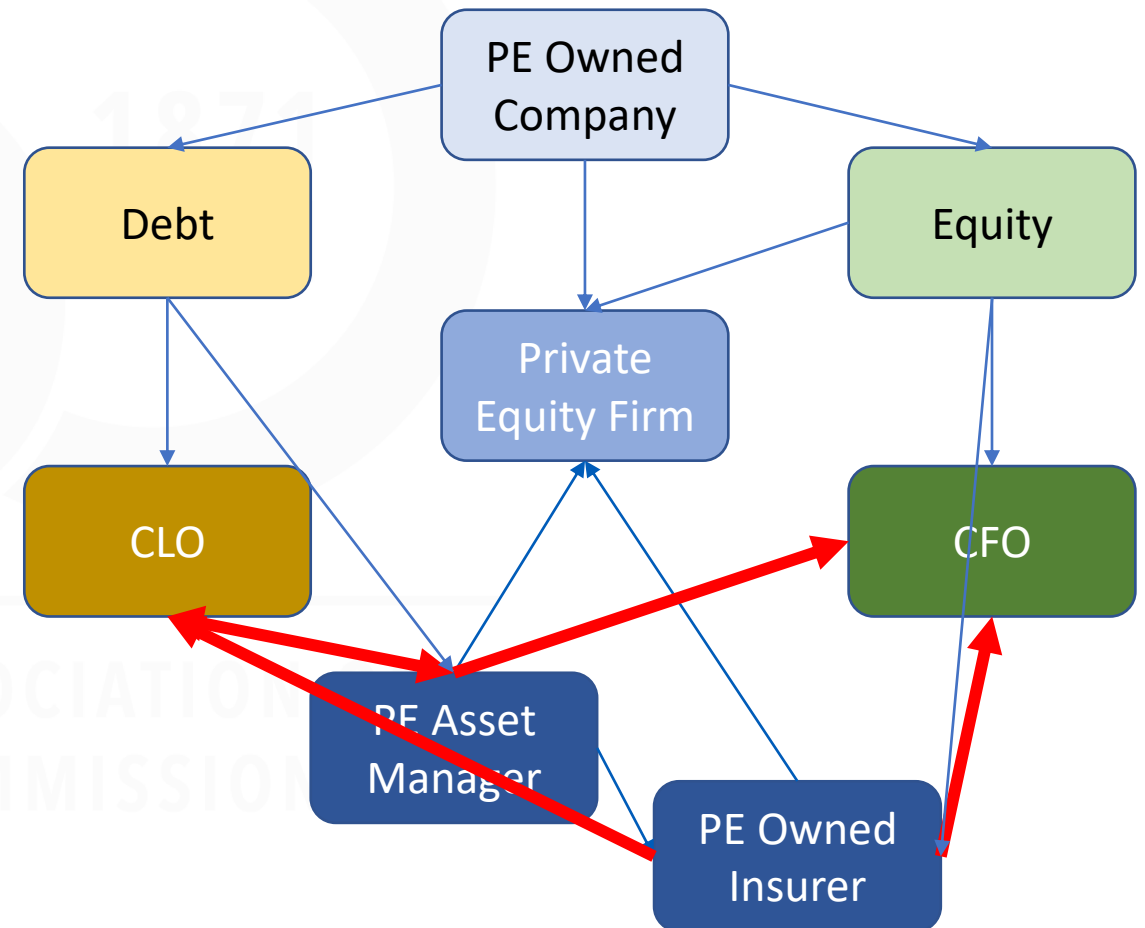
- The PE business model has transitioned over the years from restructuring companies for profit to fee generation.
- PE companies seek to generate fees at every level of their investment from the underlying corporate to CLOs to managing assets for insurers.
- The PE owned insurance company stands as the ultimate risk taker for the PE pipeline.
- However, the interconnected relationships are not always clear.





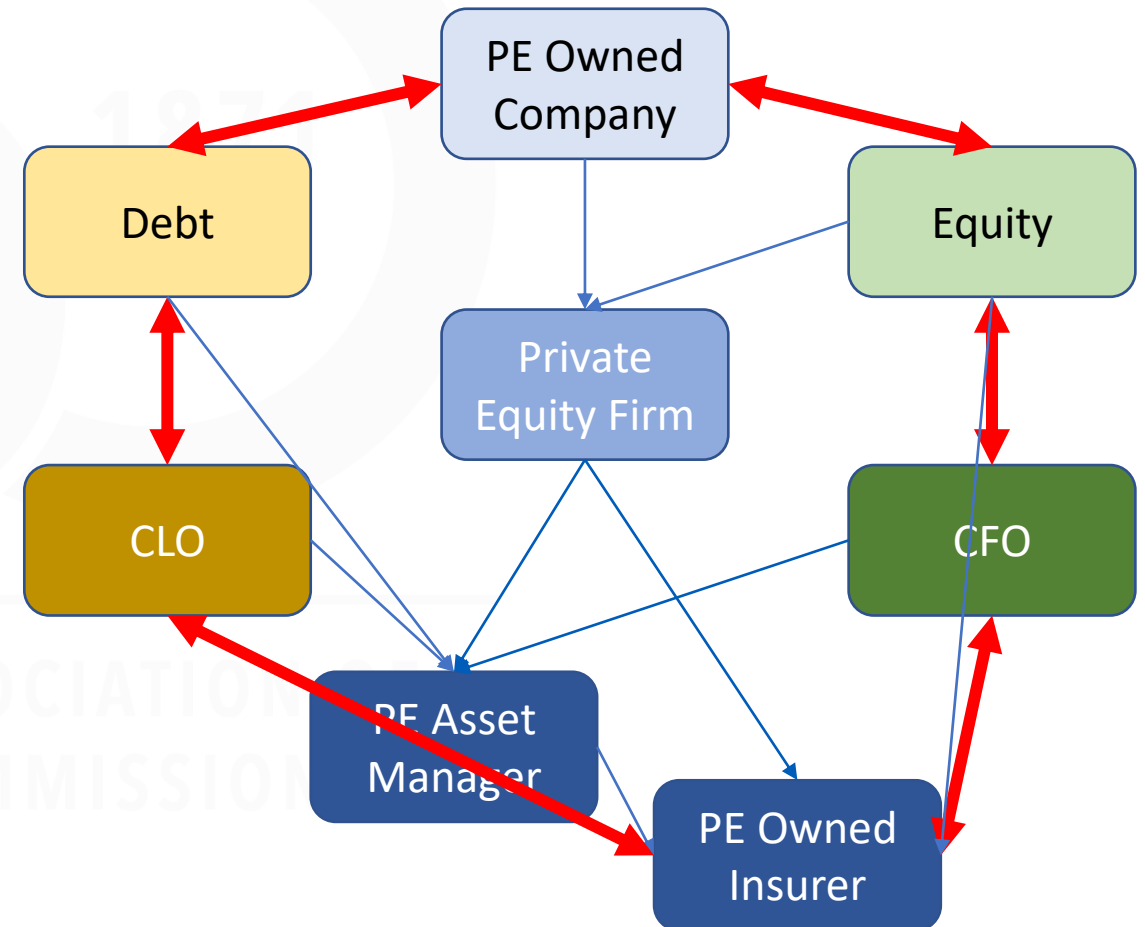
# Affiliates – 1<sup>st</sup> Degree

- 1<sup>st</sup> Degree Affiliates are structured vehicles which are managed by the PE firm's asset management affiliate.
- It is common for PE owned firms to report affiliated managed CLOs and structured products as "unaffiliated".



# Affiliates – 2<sup>nd</sup> Degree

- 2<sup>nd</sup> degree affiliates are the debt or equity of PE owned companies held by CLOs or CFOs (affiliated or unaffiliated) held by the insurer.
- For example, we found that for one large insurer group that approximately 70% of their CLOs hold some exposure to their portfolio companies.





# Staff Proposals to Address PE Ownership

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# Establish New Definition for PE Owned Insurer

- Based on the stated principles, the definition of PE revolves around the fee generation.
- **“Financial Entity Owned Insurer”** is a regulated insurer which is controlled by or has a long term investment management agreement with an entity which:
  1. Derives the majority of its revenue through the management of or investment in financial assets.
  2. Is not itself a regulated insurer.
  3. Has some minimum AUM.



# Broaden Affiliate Reporting

- Bolster the definition of Affiliate to include entities managed by an affiliate of the “Financial Entity Owned Insurer”.
  - 1<sup>st</sup> Degree Affiliates – CLO managers
- Require that “Financial Entity Owned Insurer” reporting of affiliated entities owned by an asset in an insurer's portfolio.
  - 2<sup>nd</sup> Degree Affiliates – e.g. loans to companies owned by a CLO in an insurer’s portfolio.



# Strengthen Affiliate Reporting

- More transparent disclosure of fees paid / accruing to 1<sup>st</sup> and 2<sup>nd</sup> degree affiliates.
- Disclosure of AUM of all affiliates.
- Identify investments in the investment schedules where there are other relationships with 1<sup>st</sup> or 2<sup>nd</sup> degree affiliates.
  - E.g. the investment was structured by the affiliate.