



CLO Residual Updates

Who this impacts:

U.S. NAIC statutory filers (health, P&C)

Timeline:

At the NAIC Spring 2024 meeting, regulators proposed to separate residual tranches in Schedule BA for P&C insurers. A final vote is expected to occur before the end of June. Projected implementation would be in 2024.

Description:

The NAIC proposed changes to the reporting of residual interests held by health and P&C companies and reported on Schedule BA.

Currently, collateralized loan obligation (CLO) equity tranches are categorized as common stocks and receive a 20% capital charge. The proposed changes would separate the reporting of CLO equity from common stocks. This would allow regulators more flexibility to set different capital charges for CLO equity positions if needed in the future.

Implication and next steps:

We believe insurers should understand their exposure to structured securities. Once the residual tranche reporting structure is adopted, the P&C committee will discuss options for what capital charge to apply:

1. Keep the current 20% charge
2. Increase it to 45% to be aligned with the life insurance capital rules, starting in 2024
3. Wait for the Risk-Based Capital (RBC) Working Group to complete its analysis and studies before proposing any changes to the P&C capital formulas

Prior to the NAIC Spring 2024 meeting, option #3 was the expected outcome. However, it now appears that option #2 is the more likely.

Source: National Association of Insurance Commissioners, 2024.