October 2, 2026

VIA EMAIL

Kevin Clark, Chair
Statutory Accounting Principles (E) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106

Re: Agenda Item 2026-10 - SSAP No. 26, Bonds (Proposed Treatment of Embedded Asset-Liability Management Risk in Asset-Backed Securities)

Dear Mr. Clark:

LSTA, Inc. ("LSTA")[1] and the Alternative Credit Council ("ACC")[2] respectfully submit these comments on Agenda Item 2026-10, which the Statutory Accounting Principles (E) Working Group ("SAPWG" or the "Working Group") exposed for comment at the 2026 Summer National Meeting. Both organizations' members include, and act as counterparties to, many of the life insurers subject to the Statement of Statutory Accounting Principles ("SSAP") framework, and both organizations have a strong interest in ensuring that the principles-based bond definition ("PBBD") continues to function predictably for the structured credit markets our members build, manage, and invest in.

We understand the regulatory objective underlying Agenda Item 2026-10: SAPWG and state insurance regulators should have the analytical tools and transparency needed to monitor asset-liability management ("ALM") risk. We offer the recommendations below to help the Working Group achieve its stated objective with precision.

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[1] LSTA, Inc. is a not-for-profit trade association that has been the leading advocate for the U.S. corporate lending market since 1995. LSTA's mission is to promote a fair, orderly, efficient and growing corporate loan market while advancing and balancing the interests of all market participants. Our 600+ member institutions include commercial banks (ranging in size from GSIBs to community banks), investment banks, broker-dealers, asset managers, and institutional lenders, as well as law firms and market service providers. For more information, visit www.lsta.org.

[2] The Alternative Credit Council (ACC) is a global body that represents asset management firms in the private credit and direct lending space. It currently represents 250 members that manage over US$2 trillion of private credit assets. The ACC is an affiliate of AIMA and is governed by its own board, which ultimately reports to the AIMA Council. ACC members provide an important source of funding to the economy. They provide finance to mid-market corporates, SMEs, commercial and residential real estate developments, infrastructure, and the trade and receivables business. The ACC's core objectives are to provide guidance on policy and regulatory matters, support wider advocacy and educational efforts and generate industry research to strengthen the sector's sustainability and wider economic and financial benefits.

I. Background on insurance investments in structured credit and impact of capital charges

Life insurers are among the largest institutional holders of structured credit vehicles that finance non-investment-grade businesses. As of year-end 2024, U.S. insurers held approximately $276.8 billion in CLOs - more than double their 2018 exposure - with life insurers accounting for 82% of that total (approximately $226.5 billion).[3] CLO holdings represented roughly 5.1% of total insurer bond holdings and 3.1% of total cash and invested assets industry-wide, with exposure concentrated among the largest institutions.[4] The treatment of these instruments under the PBBD therefore has an outsized effect both on insurers' investment portfolios and on the cost and availability of credit to the borrowers who depend on this financing.

Most of this exposure is high-quality credit and has performed accordingly. Approximately 90% of insurers' CLO holdings carry investment-grade ratings (39% AAA, 22% AA, 15% A, and 12% BBB), with only about 2% rated below investment grade.[5] This is not simply a product of a benign credit cycle: S&P Global Ratings' 30-year tranche default study found that investment-grade-rated CLO tranches experienced a cumulative default rate of only 0.3% from 1994 through the first quarter of 2024, with those defaults concentrated almost entirely in pre-financial-crisis vintages issued under structural protections weaker than those standard in CLOs today, and confirmed that no CLO tranche rated AAA or AA has ever defaulted.[6] This performance record reflects the structural protections - subordination, overcollateralization and interest-coverage triggers, and typically five-year-or-shorter reinvestment periods - built into conventional, single-collateral-type CLOs, which are not the structures Agenda Item 2026-10 is aimed at.

The stakes of the bond/non-bond determination under Paragraph 9 are unusually high because the accounting classification drives the risk-based capital ("RBC") charge mechanically, with no gradation in between. Life RBC bond factors currently range from roughly 0.4% for the highest-quality designation (NAIC 1) up to 30% for the lowest bond designation (NAIC 6); a security that instead fails the PBBD and is reported on Schedule BA generally defaults to the same approximately 30% factor applied to unaffiliated common stock, unless the insurer subsequently submits the failed bond to the SVO and receives a designation based on their analysis of the credit risk. In addition, the NAIC has separately developed a dedicated 45% pretax factor for CLO residual/equity tranches.[7][8] In practical terms, a well-subordinated, investment-grade-rated debt tranche carrying a 0.4% RBC factor today could see its capital charge increase 75x to well over 100x if it is found to contain "significant" embedded ALM risk and loses bond treatment - a consequence entirely disconnected from any change in the security's actual credit quality or collateral performance.

Because SSAP classification drives RBC charges mechanically, an ambiguous standard is not merely an accounting problem - it is a capital problem. Absent workable, administrable criteria, economically similar structures will be classified inconsistently across filers, producing divergent RBC charges for

[3]NAIC Capital Markets Bureau, U.S. Insurers' CLO Exposure at Year-End 2024 (2025).
[4]NAIC, Private Credit Issue Brief.
[5]NAIC Capital Markets Bureau, U.S. Insurers' CLO Exposure at Year-End 2024 (2025).
[6]S&P Global Ratings, CLO Spotlight: Thirty Years Strong - U.S. CLO Tranche Defaults From 1994 Through First-Quarter 2024 (2024).
[7]NAIC Life Risk-Based Capital Instructions, Investment Risk-Based Capital Factors.
[8]NAIC Risk-Based Capital Investment Risk and Evaluation (E) Working Group, Agenda and Materials (June 23, 2026).

identical risk and undermining the cross-industry comparability RBC is designed to ensure. That uncertainty carries real consequences: it risks forcing sales of legacy holdings into an illiquid secondary market precisely when conditions are already stressed, and it injects unnecessary uncertainty into new-issuance and portfolio-construction decisions for a market on which insurers, CLO managers, and private credit fund managers depend for stable, long-term financing.

II. Recommendations

Determining whether a structured security with a fixed-duration, self-terminating reinvestment period results in significant ALM risk requires significant judgment and analysis. We recommend that SAPWG establish a two-stage process to determine what constitutes significant embedded ALM risk. The first stage would be to establish a rebuttable presumption of significant ALM risk. If a structure meets the criteria for the practical expedient described below, then that structure would not be deemed to pose significant embedded ALM risk and would continue to qualify as a bond. If it does not meet either criterion, the structure would need to be analyzed under the criteria in the second recommendation, which adds relevant factors to subparagraph 9.d to determine whether the rebuttable presumption can be rebutted.

Recommendation 1 – Establish a Rebuttable Presumption Regarding Significant Embedded ALM Risk

As a practical expedient, any structure that meets either of the following criteria would not be considered to create significant embedded ALM risk:

(i) the reinvestment period, measured from the closing date of the transaction, does not exceed seven years; or

(ii) the weighted average life (WAL) of the underlying assets exceeds 30-50%[9] of the vehicle's effective maturity.

Seven years reflects the staff memorandum's own reference to reinvestment periods of five years or less as "not uncommon" for conventional structured credit.[10] A seven-year threshold would de-scope well-established structures with reinvestment periods of five years or less, including most CLOs, while accommodating structures that fall modestly above the five-year mark and ensuring that testing and the associated regulatory review are applied only to true outliers. This threshold reduces regulatory burden for insurers and state regulators, and gives insurers the predictability necessary to avoid disruption to conventional asset classes they already hold. By contrast, the appropriate WAL threshold requires further empirical analysis. We propose 30–50% as a starting range to be calibrated through a data-driven process.

These two tests are designed to be both workable in practice and consistent with how the PBBD already approaches structural protection. These two tests give preparers, auditors, and regulators a predictable, administrable path to resolve the overwhelming majority of conventional securitizations - including CLOs, which, as noted above, make up a large, high-credit-quality, and historically well-performing share of insurers' structured credit portfolios - without requiring a full facts-and-circumstances review of each

[9]. Exact percentage to be determined by empirical analysis.

[10]NAIC Statutory Accounting Principles (E) Working Group, Agenda Item 2026-10, SSAP No. 26 - Embedded ALM Risk, Staff Memorandum, content.naic.org/sites/default/files/inline-files/26-10-ssap-no-26-embedded-alm-risk.docx.

transaction, while preserving full scrutiny for the structures the project targets.

Recommendation 2 - Require Structural Mitigants to Be Included When Determining What Constitutes "Significant" ALM Risk

As drafted, the "could be impacted by changes in reinvestment interest rates or investment spreads" test is so broad and undefined that it could be read to compel a "significant" finding based on a wide variety of theoretical concerns, such as the existence of reinvestment-rate sensitivity, without regard to whether the transaction's own structure has already priced in, hedged, or subordinated that risk. We recommend that subparagraph 9.d. require that, before a reporting entity or examiner concludes that embedded ALM risk is "significant," the analysis consider what structural mitigants are present in the transaction, including but not limited to:

(i) the reinvestment period is fixed at issuance and cannot be unilaterally extended by the manager, sponsor, or servicer;

(ii) the reinvestment period is followed by mandatory - not merely permitted - amortization of the debt tranches;

(iii) the transaction includes overcollateralization and/or interest-coverage triggers that force early amortization upon collateral deterioration during the reinvestment period;

(iv) interest-rate or basis hedges executed at the transaction level;

(v) subordination sized with reference to, and sufficient to absorb, reasonably foreseeable reinvestment-rate or spread-related shortfalls - not merely credit losses; and

(vi) active portfolio and ALM governance, including manager modeling and stress-testing of reinvestment risk.

We recommend that SAPWG follow the same principles-based approach that is used elsewhere in the PBBD, in that the examples above of structural mitigants should not be considered an exhaustive list. A strength of the principles-based approach is that it allows for consideration of what structural mitigant is appropriate and needed for each specific type of underlying asset. For instance, overcollateralization may be sufficient for some types of underlying collateral, whereas subordination and/or hedging might be more appropriate for other types of assets.

Incorporating appropriate ALM mitigants aligns with how the PBBD already treats credit risk elsewhere and avoids the perverse incentives an indiscriminate test would create. The PBBD's existing "substantive credit enhancement" concept in Paragraph 10 already asks whether subordination, overcollateralization, or guarantees put the bondholder "in a different economic position" than a direct holder of the collateral would be. The same principles-based, facts-and-circumstances methodology should apply to embedded ALM risk. A structure with a long legal final maturity but hard triggers that force rapid amortization well before any meaningful reinvestment-rate exposure could materialize presents a fundamentally different risk profile than a similarly-tenored structure with no such protections, and the rule should not treat the two identically.

A mitigant-blind rule creates perverse incentives on both sides of the transaction. Sponsors and managers have less reason to build in costly protections that the test will not recognize. And insurers have correspondingly less reason to select for, or pay up for, better-protected structures, since a hedged, over-

collateralized, actively managed deal receives the same Schedule BA treatment as one with none of those features - pushing capital toward whatever structure technically avoids triggering the standard's literal wording, rather than toward the structure with the best actual risk profile.

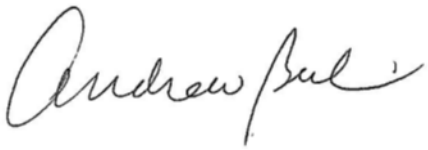
This recommendation is complementary to Recommendation 1 and does not depend on its outcome. Duration-mismatched structures should evaluate mitigants before concluding that risk is "significant," because two structures with the same nominal duration gap can present very different practical ALM risk depending on their protective features.

III. Conclusion

We appreciate SAPWG's willingness to engage with industry on these complex structural questions, and we share the Working Group's interest in ensuring that insurers hold appropriate capital against genuine embedded ALM risk. We believe the recommendations above would allow the Working Group to achieve that objective precisely, while avoiding unintended consequences for the broader and largely unrelated market for conventional structured credit on which insurers, and the companies that depend on this financing, rely. We would welcome the opportunity to discuss these comments further as this project moves forward.

Sincerely,

LSTA, INC.



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