



January 29, 2026

Risk-Based Capital Investment Risk and Evaluation Working Group
Capital Adequacy (E) Task Force
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Via Email

Re: Comments on American Academy of Actuaries' December 15, 2025, Presentation titled C-1 Subcommittee Update on CLO C-1 Factors Modeling

Dear Members of the Risk-Based Capital Investment Risk and Evaluation (RBC-IRE) Working Group:

We appreciate the opportunity to provide comments on the AAA's December 15, 2025, presentation to regulators regarding the ongoing development of C-1 factors for Collateralized Loan Obligations (CLOs). We commend the AAA C-1 Subcommittee, chaired by Stephen Smith, for its collaborative efforts with the NAIC's Structured Securities Group (SSG) to refine a modeling approach that better reflects the risk characteristics of CLOs held by insurers. This work represents a significant improvement over prior methodologies, and we support its continued advancement.

AAA vs SSG CLO Model: The Academy model uses a large-scale stochastic simulation with 10,000 equally weighted economic scenarios. This generates robust default vectors for the underlying loans, which are then fed through detailed waterfall mechanics (via CDO-Net) to simulate tranche performance. It explicitly measures tail risk using a Conditional Tail Expectation (CTE-90) approach, averaging losses across the worst 10% of outcomes, translating to 17 scenarios.

In contrast, the SSG approach relies on only 10 deterministic scenarios, which are artificially probability-weighted and back-solved primarily to enforce strict equivalence between the CLO's vertical slice RBC charges and the weighted-average charges of the underlying loan pool. This limits visibility into genuine tail risk, reduces emphasis on stochastic variation, and can mask tranche-specific sensitivities by scaling results to loan-pool averages.

We believe the AAA framework is "largely there" and represents the best path forward for establishing fair and accurate capital charges. Therefore, we urge the Working Group not to

revert to less sophisticated models, such as the SSG approach or a uniform fallback percentage, as these would not adequately capture the diversified and structured nature of CLOs.

Recommendations on Assumptions and Refinements: We note the Academy model's sensitivity to key assumptions, some of which still need adjustments to be fully calibrated, which can significantly influence outcomes. In particular:

- *Loss Given Default (LGD):* The proposed adjustment from 27% to 36% represents a notable increase that could materially impact capital charges. We appreciate the Academy's transparency in highlighting assumption dependencies and look forward to further details in the February 10, 2026, presentation, including the appendix on underlying assumptions.
- *Prepayments:* We appreciate the Academy's sensitivity analysis regarding prepayment speeds given prepayments occur across all market conditions, including stressed conditions and periods of elevated defaults. We recommend the Academy consider a more moderate prepayment assumption that reflects historical floors observed during stressed periods to avoid overstating tail risk and capital charges.
- *Reinvestment Price:* Assumptions around reinvestment should be reviewed to align with market realities, ensuring they do not unduly penalize CLO structures. Notably, the par assumption departs materially from market realities. We suggest incorporating real-world data to refine these elements, recognizing the assumption-dependent nature of the model (as noted with at least five key variables that could alter results).
- *Probability of Default (PD):* While not highlighted in the December 15 presentation, we believe there could be significant improvements in PD modeling. We encourage the AAA to couple consideration of changes to recoveries with revisions to the Academy's current probability of default assumptions. These are currently based on US corporates of all seniorities. Using historical experience of US BSL loans, which have exhibited lower relative defaults than bonds, would be more appropriate and realistic.

Anticipated Next Steps and Collaboration: We eagerly await the early 2026 presentation of residual tranche results, portfolio adjustment factors, model refinements, and potential comparable attributes. The full application of the model to the broader universe of CLOs owned by life insurers, as planned for February 10, 2026, will provide greater certainty and enable more precise feedback. In the interim, we are prepared to offer technical input from our CLO subject matter experts as well as data to support assumptions that align with observable market dynamics.

Thank you for your dedication to developing risk-based capital standards that promote a stable and competitive insurance industry. We stand ready to engage further and provide any additional information needed.

Sincerely,

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