Life Risk Based Capital

MBA's advocacy for reduced risk-based capital standards.

BACKGROUND

Life insurance companies are subject to regulation by state insurance regulators. That regulatory framework includes Risk-Based Capital (RBC) standards. RBC standards specify the minimum amount of capital a life company must hold on its balance sheet for various categories of business activities.

State insurance regulators' RBC standards generally are identical to model standards established by the National Association of Insurance Commissioners (NAIC). Therefore, MBA actively works with the NAIC to foster risk-based capital rules that appropriately enable life companies to continue to be a stable source of capital for commercial real estate.

REAL ESTATE INVESTMENTS PROPOSAL

MBA worked with the NAIC and its Investment (E) Risk-Based Capital Working Group to secure a reduction for the RBC charge for life company holdings of equity real estate in 2022. Briefly, the proposal modifies the life insurer risk-based capital treatment of real estate investments as follows:

- **Schedule A real estate assets.** The previous C-1 factor of 15% is based on 60% of the common stock factor, adjusted for taxes. The proposal is based on historical experience as to real estate assets and would reduce the C-1 factor to a lower level, e.g., 10%.

- **Schedule BA real estate assets.** The previous C-1 factor of 23% is based on the C-1 factor for Schedule A real estate assets, multiplied by 150%. The proposal would reduce that multiplier to 100% (and would incorporate proposed changes to the C-1 factor for Schedule A real estate assets).

- **Encumbrances.** The prior methodology for encumbrances incorporates risk-based capital treatments for (1) real estate assets and (2) commercial mortgages. The proposal would not change the methodology but would update its application to reflect the proposed changes to the C-1 factor for Schedule A real estate assets, and the risk-based capital treatment of commercial mortgages adopted in 2013.

- **Market-value adjustment.** Previously, no amount of unrealized gains was recognized for risk-based capital purposes. The proposal would recognize some proportion (2/3) of unrealized gains to reflect the impacts of market value vs. book value on the ability to absorb loss.

RECENT NAIC EFFORTS

In April 2023, the NAIC Life Risk-Based Capital (E) Working Group adopted **revisions** to RBC factors for CM6 and CM7 mortgages. MBA and the American Council of Life Insurers (ACLI) presented the revisions jointly to the working group in late 2022 and provided the economic analysis requested by the working group outlining the effects of the proposed changes.

The revisions harmonize the RBC factors for CM6 and CM7 mortgages with the RBC factors for Schedule A and Schedule BA real estate investments, as recently adjusted. They also harmonize the formulas used to apply RBC factors to performing and non-performing mortgages, by eliminating the adjustments for write-downs currently included in the non-performing mortgages formula.

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