Attachment G

Financial Security for Life

ACLI Proposal on RBC Treatment of Repurchase Agreements

August 2023

Executive Summary

With minor reporting modifications, industry proposes to align the 1.26% C-0 charge for conforming repurchase agreements (repo) with the 0.2% C-0 charge for conforming securities lending programs

The capital alignment proposal is supported by:

- Enhanced Blanks reporting for repo since 2018 organized by SAPWG has improved transparency
- Proposed expanded disclosures in RBC Instructions and General Interrogatories address liquidity risk in repo, the rationale for the C-0 charge
- Counterparty bankruptcy protections in sec lending and repo are nearly identical
- Current RBC framework disincentivizes insurers to diversify counterparty exposure/financial interconnectedness away from primary dealers

ACLI Proposal for Repo RBC

Establish "conforming program criteria" option for repurchase agreements through the General Interrogatories. A "conforming" program is managed against clear operational and risk guidelines, including that the collateral margin applied to transactions is within the industry standard. Reporting insurers can attest compliance for the conforming portion of their repo program.

Proposed C-0 RBC for conforming repo programs is the sum of:

- 0.20% charge for conforming repo assets
- Additional RBC applied to insurer's net counterparty exposure (Slide 9)

All other repo programs maintain existing 1.26% C-0 RBC charge

[1] The ACLI proposal is strictly limited to repurchase agreements and does not include similar contracts such as reverse repo or dollar rolls.

Proposal Benefits

- Closer alignment of capital charges between securities lending and repo transactions would incentivize diversifying sources of short-term funding
- Diversification would reduce exposure to Primary Dealers and the idiosyncratic risk associated with bank balance sheet management
- Diversification would encourage stable funding from alternative sources such as state sponsored funds, asset managers and money market funds
- Non-punitive access to alternative funding options improves insurers' ability to sustain funding through stressed market environments, reducing the risk of asset fire sales
- NAIC has reported expanded use of repurchase agreements among Insurers over time

Current Statutory Reporting for Repo: Foundation for Proposed Enhancements

Current statutory reporting for repo occurs primarily through footnotes

- The maximum and ending amount of securities sold under repurchase secured borrowing by book adjusted carrying value and fair value in footnote 5 F (5) b.
- Aggregate collateral reinvestment amounts by remaining maturity by fair value footnote 5 F (10).
- Amount of securities sold under repurchase secured borrowing by book adjusted carrying value in the General Interrogatories - 26.21.

Proposed Reporting Enhancements

Industry proposes a General Interrogatories reporting enhancement to allow regulators to validate that insurer repo programs meet the “conforming” definition.

Industry proposes to mimic General Interrogatory line 25.04/.05 to reflect repurchase amounts, showing the amount of collateral received for conforming programs as well as amounts for other repo programs. Footnote 5 F (5) provides the amount of securities sold and footnote 5 F (7) identifies the reinvested collateral. Would require expansion of LR17 to include both Conforming and Other Repurchase Agreement rows.

Industry also proposes to replicate the existing criteria for sec lending conforming programs in the RBC Instructions with parallel criteria for conforming repo programs.

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Proposed General Interrogatories Enhancement

Statement			Notes	Factor	Amount	Status
General Interrogatories	25.04	For the reporting entity's securities lending program, report amount of collateral for conforming programs as outlined in the Risk-Based Capital Instructions.			500	Current
	25.05	For the reporting entity's securities lending program, report amount of collateral for other programs.			0	Current
	25.06	For the reporting entity's repurchase agreement program, report amount of collateral for conforming programs as outlined in the footnote 5 F (7). Repurchase Agreements Transactions for as Secured Borrowing.	Fair Value Measure - Cash Collateral Received		98	Proposed
	25.07	For the reporting entity's repurchase agreement program, report amount of overcollateralization for conforming programs, as the difference between footnote 5 F (5) and 5 F (7), Repurchase Agreements Transactions for as	Fair Value Measure - Cash Collateral Received minus Fair Value of Collateral Sold		2	Proposed
	25.08	For the reporting entity's repurchase agreement program, report amount of collateral for other programs.			0	Proposed
LR17	(1)	Loaned to Others - Conforming Securities Lending Program	General Interrogatories Part 1 Line 25.04	0.20%	500	Current
	(2)	Loaned to Others - Securities Lending Programs - Other	General Interrogatories Part 1 Line 25.05	1.26%	0	Current
	(3)	Loaned to Others - Conforming Repurchase Agreement Program Collateral	General Interrogatories Part 1 Line 25.06	0.20%	98	Proposed
	(4)	Loaned to Others - Conforming Repurchase Agreement Program Overcollateralization	General Interrogatories Part 1 Line 25.07	C-1 BBB	2	Proposed
	(5)	Loaned to Others - Repurchase Agreement Programs - Other	General Interrogatories Part 1 Line 25.08	1.26%	0	Proposed

Proposed RBC Instructions Enhancement

Line (2)

Repurchase programs (similar in nature to Securities Lending) that have all of the following elements are eligible for a lower off-balance sheet charge:

1. A written plan adopted by the Board of Directors that outlines the extent to which the insurer can engage in securities lending like activities (under repurchase agreements) and how cash collateral received will be invested.

2. Written operational procedures to monitor and control the risks associated with securities lending/repurchase agreements. Safeguards to be addressed should, at a minimum, provide assurance of the following:

a. Documented investment guidelines, including, where applicable, those between lender and investment manager with established procedure for review of compliance.

b. Investment guidelines for cash collateral that clearly delineate liquidity, diversification, credit quality, and average life/duration requirements.

c. Approved borrower lists and loan limits to allow for adequate diversification.

d. Holding excess collateral with margin percentages in line with industry standards, which are currently 98%.

e. Daily mark-to-market of lent securities and obtaining additional collateral needed to ensure that collateral at all times exceeds the value of the loans to maintain margin of 98% of market.

f. Not subject to any automatic stay in bankruptcy and may be closed out and terminated immediately upon the bankruptcy of any party.

3. A binding repurchase agreement (standard “Master Repurchase Agreement” from Securities Industry and Financial Markets Association) is in writing between the insurer, or its agent on behalf of the insurer, and the borrowers.

4. Acceptable collateral is defined as cash, cash equivalents, direct obligations of, or securities that are fully guaranteed as to principal and interest by, the government of the United States or any agency of the United States, or by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation and NAIC 1-designated securities. Affiliate-issued collateral would not be deemed acceptable. In all cases the collateral held must be permitted investments in the state of domicile for the respective insurer.

Application of RBC Charges

- 0.20% C-0 Repurchase RBC Factor applied to footnote 5 F (7) ending balance for collateral received under secured borrowing (or the conforming amount determined on the proposed enhancement)
- Additional RBC charge applied to the 2% "Overcollateralization Amount"
    - Overcollateralization Amount equals the difference in statement balances for the above-mentioned footnote 5 F (7) ending balance for collateral received under secured borrowing net of the statement balance for Footnote 5 F (5) defining the fair value ending balance for securities sold under repurchase secured borrowing
    - The 2% Overcollateralization Amount is akin to the unsecured credit exposures insurers assume in their bond portfolios. Repo counterparts, often government-only money funds, are typically rated AA or AAA. To be conservative, the C-1 RBC factor for bonds rated BBB (~1.5%) is applied to the Overcollateralization Amount. Counterparties rated below BBB would be ineligible for a conforming repo program

Appendices

- Repo transaction structure
- Previous Reporting Enhancements and Impact
- Current Repurchase Reporting Detail

Repo Transaction Structure

- Bi-Lateral - Direct agreement between two counterparties whose custodian banks settle the trade
- Tri-Party - A third-party custodian bank settles the trade between two counterparties
- Collateral - Repurchase agreement standard cash collateral levels are 95%-98% of the loaned securities market value
  - Insurer considers the 2-5% as ‘over-collateralization’ to the borrower
  - The ‘over-collateralization’ is a component of the proposal

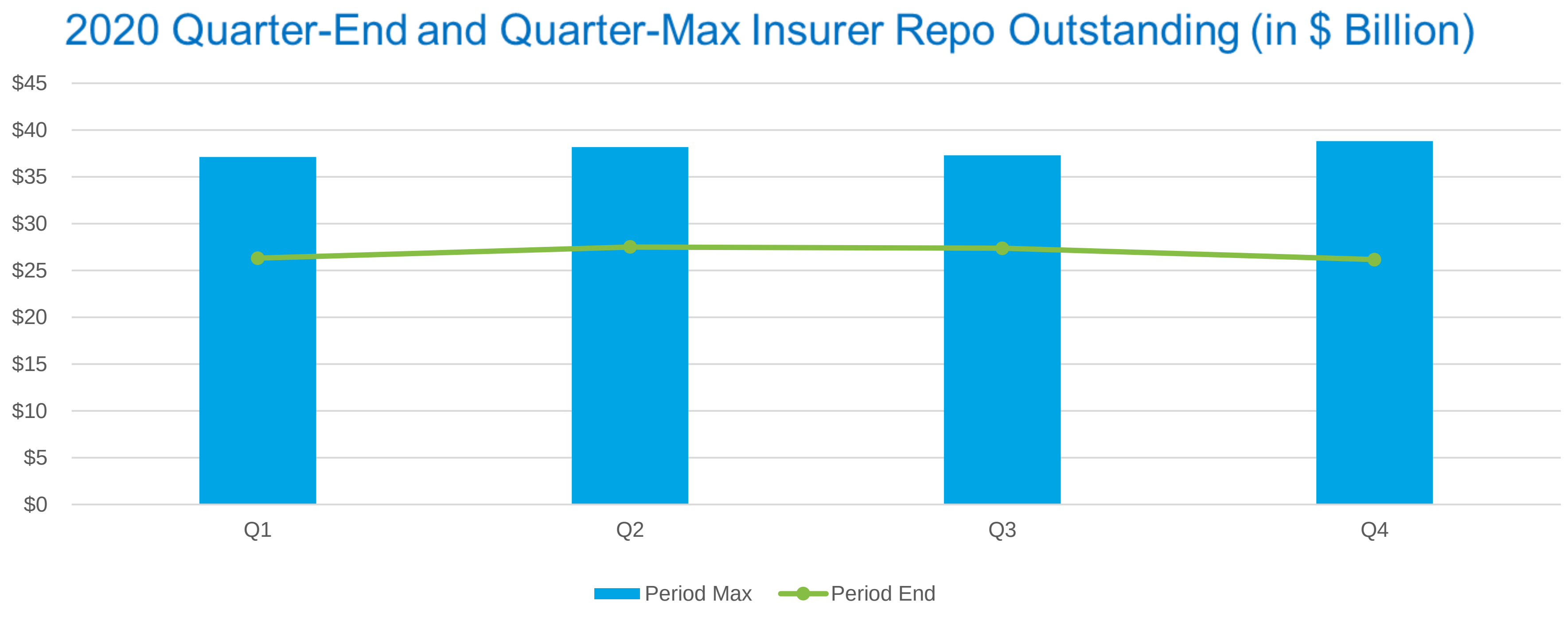
Reporting Enhancements

- Industry committed to providing expanded reporting
  - 2015 – The FSB developed process for collecting and aggregating repo data
  - 2017 – The SAPWG approved repurchase agreement disclosure requirements
  - 2018 – The BLANKS Working Group updated the footnote instructions and schedule layout

Limited "Window Dressing"

The chart below illustrates the limited variability of insurer repo activity:

- Highest quarter-end repo outstanding was only 5% greater than year-end
- Intra-quarter maximum outstandings averaged 40% higher than quarter-end



Current Repurchase Reporting Detail

1. Summary
2. Repurchase by type
3. Repurchase by maturity bucket
4. Securities sold that resulted in default
5. Securities sold under repurchase secured borrowing by inter-quarter maximum amount and ending balance
6. Securities sold under repurchase secured borrowing by NAIC designation
7. Collateral received under secured borrowing by inter-quarter maximum amount and ending balance
8. Collateral received under secured borrowing by NAIC designation
9. Allocation of aggregate collateral by remaining contractual maturity
10. Allocation of aggregate collateral reinvested by remaining contractual maturity
11. Liability to return collateral under secured borrowing by inter-quarter maximum amount and ending balance