# Risky Business: NAIC's Proposal to Limit Disclosure of Risk-Based Capital

**August 6, 2024**

## NAIC PROPOSAL

A proposal by the National Association of Insurance Commissioners (the "NAIC") could have a significant impact on how insurance companies publicly disclose their Risk-Based Capital ("RBC") ratios. At a December 2023 meeting, certain regulators expressed their views that RBC information is a confidential regulatory tool meant to evaluate whether regulatory action is required based on a company's total adjusted capital falling below certain prescribed levels. In the view of these regulators, RBC ratios should not be used for any other purpose. In response, the NAIC Capital Adequacy (E) Task Force (the "CATF") formed an RBC Purposes and Guidelines Ad Hoc Subgroup (the "RBC Ad Hoc Subgroup") to recommend revisions to the Risk-Based Capital Preamble (the "RBC Preamble") to clarify and emphasize the intended uses of RBC. The RBC Ad Hoc Subgroup's work culminated in the release of a draft proposal (2024-16-CA) by the CATF in April 2024 which revised the RBC Preamble to, among other things, delineate additional examples of prohibited public disclosure of RBC levels including in "press releases, earnings releases, webcast materials, or any other earnings presentations or webcasts." The proposed edits were thereafter exposed for comments until May 30, 2024.

While the RBC Preamble has for many years contained language restricting the public use of RBC, including a prohibition on the "making, publishing, disseminating, circulation or placing before the public . . . statement[s] containing an assertion, representation or statement with regard to the RBC levels of any insurer," many companies and third parties (including analysts) have published RBC information over the years. Among other reasons, this practice was supported by the fact that such information was already disclosed in the publicly available annual statutory financial statements filed by insurers with state regulators and with the NAIC. In light of the proposed edits to the RBC Preamble, however, it is anticipated that the two reported RBC components (authorized control level and total adjusted capital) that have historically been included in statutory financial statements may be removed from the annual statement's five-year historical pages. This would call into doubt the premise on which insurance holding companies publish RBC levels in other disclosure.

The majority of the feedback to proposal 2024-16-CA received by the NAIC opposed the additional restrictions on public disclosure of RBC levels:

- The American Academy of Actuaries focused on the importance of RBC transparency inasmuch as providing a transparent basis of evaluating insurance company solvency is essential for an insurance regulatory regime, and aligned with the globally accepted framework for insurance supervision.

- The American Council of Life Insurers noted that the ability of companies to share their RBC ratio in public forums has significantly strengthened public perception of the U.S. state-based regulatory system of insurance companies, e.g., during and after the financial crisis of 2008–2009.

- Two market participants cautioned that making RBC confidential would make state regulation an outlier and in contravention of international standards. Moreover, proposed preamble language that frames RBC as unreliable for well-capitalized companies may be perceived as calling into question its efficacy for purposes of regulatory action against weakly capitalized companies.

## CONFLICT WITH CURRENT DISCLOSURE PRACTICES

If adopted as proposed, the NAIC's proposal to prohibit the disclosure of RBC-related information would conflict with historical disclosure practices and certain accounting and regulatory requirements relevant to insurance companies. For example, the proposal would arguably conflict with Generally Accepted Accounting Principles ("GAAP") Accounting Standard ASC 944-50-50-1, which requires insurance entities and entities controlling U.S. insurance subsidiaries to disclose in their financial statements the amount of statutory capital and surplus, the amount of statutory capital and surplus required to satisfy regulatory requirements and the nature of statutory restrictions on the payment of dividends to stockholders.[1] Though the NAIC's proposal does not, by its

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[1] GAAP Accounting Standard ASC 944-50-50-1 states:

"Insurance entities shall disclose in their financial statements all of the following information relating to stockholders' equity, statutory capital and surplus, and the effects of statutory accounting practices on the entity's ability to pay dividends to stockholders:

a. The amount of statutory capital and surplus
b. The amount of statutory capital and surplus necessary to satisfy regulatory requirements (based on the entity's current operations) if significant in relation to the entity's statutory capital and surplus

terms, prohibit disclosure of RBC in publicly disclosed financial statements, the proposal would create tension between what public companies are *required* to disclose in their periodic reports (e.g., Forms 10-K and 10-Q) and what they are *allowed* to disclose and discuss with investors in earnings releases and earnings calls.

Indeed, many public companies with U.S. insurance company subsidiaries disclose their subsidiaries' RBC ratios, RBC ratio targets, excess capital above regulatory requirements, and similar measures in their periodic reports, as well as on earnings calls and in earnings releases. For example, a significant number of large U.S. insurance holding companies report—either quantitatively or qualitatively—whether the statutory surplus of their U.S. insurance company subsidiaries exceeds RBC ratio requirements or targets. Disclosure of these measures is often viewed as important to investors, as they help in assessing the amount of capital available to the parent holding company for dividends, share repurchases, strategic transactions and other investments in the business.

Due to the prevalence of public disclosure regarding RBC ratios, limiting public disclosure of RBC could be viewed negatively by investors and would necessitate the development of alternative measurements of capital available to the parent holding company of insurance company operating subsidiaries.

## STATUS OF THE NAIC'S PROPOSAL

Due to the feedback gathered during the comment period, the CATF concluded at its June 28, 2024 meeting that a more thorough discussion of the topic was necessary and chose to postpone any decision for the time being. We expect there to be further discussions on this proposal at the NAIC Summer National Meeting in Chicago from August 12–16, 2024. We will continue to monitor developments relating to this proposal.

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Please do not hesitate to contact us with any questions.

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c. The nature of statutory restrictions on the payment of dividends and the amount of retained earnings that is not available for the payment of dividends to stockholders."

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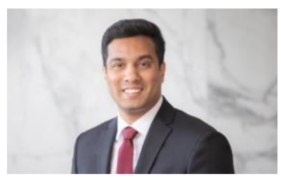

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