AMERICAN INVESTMENT COUNCIL
Growth Through Long-Term Investment

January 18, 2022

VIA ELECTRONIC SUBMISSION
Todd Sells
Director, Financial Regulatory Policy & Data
National Association of Insurance Commissioners

Re: Public Comment on NAIC Regulatory Considerations Regarding Private Equity-Owned Insurance Companies

Dear Mr. Sells:

The American Investment Council (the "AIC") is pleased that the National Association of Insurance Commissioners (the "NAIC") is seeking to further understand the relationship between private equity and insurance as outlined in the NAIC's Financial Stability Task Force (the "Task Force") considerations issued as part of the Task Force's December 7, 2021 virtual meeting and supports the review. The AIC's members also have experience with the investment needs of insurance companies, and the AIC would be pleased to be a resource to the NAIC in regard to the matters set out in the December 7, 2021 considerations.

The AIC is an advocacy, communications, and research organization established to advance access to capital, job creation, retirement security, innovation, and economic growth by promoting responsible long-term investment. In this effort, the AIC develops, analyzes, and distributes information about the private equity and private credit industries and their contributions to the U.S. and global economy. Established in 2007 and formerly known as the Private Equity Growth Capital Council, the AIC is based in Washington, D.C. The AIC's members are the world's leading private equity and private credit firms (collectively, "Alternative Asset Managers"), united by their commitment to growing and strengthening the businesses in which they invest and to helping secure the retirements of millions of pension holders and insurance policyholders.[1]

U.S. retirees, and the insurance companies and pension funds that invest on their behalf, are facing an unprecedented low interest rate environment even with rate increases by the Federal Reserve in the near term. Accordingly, 97% of investors

[1] For further information about the AIC and its members, please visit our website at http://www.investmentcouncil.org.

recently polled by Preqin expect allocations to alternatives to increase (81%) or remain steady (16%) by 2025.[2] With respect to insurance companies specifically, it is difficult for traditional insurance company asset managers to achieve the yield targets they have achieved historically on their debt portfolios. This leaves them with two essential choices: (1) take more risk along the yield curve in search of higher rates of return; or (2) seek other types of debt instruments that offer modestly better returns without incremental credit risk. This set of circumstances is what is driving more insurance companies to seek out the services of Alternative Asset Managers with private credit expertise to manage a portion of their assets. Insurance companies should have access to the products AIC members offer because their products are often well-suited to supporting the long-term liabilities of insurance companies. The ability to source, underwrite, and execute private credit transactions requires skill sets, experience, and scale that many insurance companies do not possess in-house. Moreover, engaging an asset manager with differentiated capabilities can be more cost efficient for an insurance company than making significant investments in an internal asset management function. By availing themselves of these advantages, insurance companies, while operating in a low-yield environment, can benefit from cost-effective sourcing and origination capabilities in specialty asset classes. This strategy results in enhanced long-term adequacy margin for policyholders, increased spread/earnings, and more competitive pricing.

There is a natural alignment between the long-dated insurance liabilities and the long-term investment approach taken by private credit managers. This alignment is also a factor in the investments that many Alternative Asset Managers are making into insurance companies themselves. In that connection, private equity's business model is predicated on building value over an extended period, including being attentive to policyholder and other stakeholder interests.[3] AIC members who work with insurance companies share insurance regulators' commitment to the long-term health of insurance companies. Private equity firms recognize the reputational aspects that may be attributed to private equity managers as they seek new opportunities. They also understand that insurance company valuations at exit depend on the long-term viability and health of insurance platforms and therefore are dis-incented from extracting short-term returns prior to exit.

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[2] *Future of Alternatives 2025* report (Preqin, 2021), available at https://www.preqin.com/insights/research/reports/preqin-special-report-the-future-of-alternatives-2025

[3] According to AM Best, "private equity firms also have infused considerable amounts of capital to spur rapid growth—a strategy that insurers do not typically execute well. In the first year of private equity ownership, 38% of companies reported increases of over 20% in capital and surplus, rising to 43% in year No. 2 and 50% in year No. 3," available at https://news.ambest.com/presscontent.aspx?refnum=30878&altsrc=9.

Private equity and private credit have a successful history of providing capital to, and managing the assets of, the U.S. insurance industry and have played a critical role in supporting that industry and insurance policyholders. Private equity has consistently outperformed traditional asset classes—such as publicly traded stocks and public mutual funds—for the past 40 plus years, including for insurance companies that make up approximately 12% of the invested capital in private equity funds.[4] While some have raised a concern that illiquid or alternative assets present increased illiquidity or other risks, studies show that illiquid or alternative assets reduce risk for a given level of return.[5] Further, while this outperformance inures to the benefit of policyholders, most of the insurance balance sheet assets managed by Alternative Asset Managers actually involve debt securities, most of which securities are investment grade or their equivalents. These securities enable insurance companies to achieve attractive risk-adjusted yields versus public debt investments. Consistent with applicable state laws and regulations, investments in private equity make up a relatively small portion of insurance balance sheets.

In addition, Alternative Asset Managers have long-term incentives and are subject to significant regulation. Private fund advisers are registered as investment advisers under the Investment Advisers Act of 1940 (the "Advisers Act") with the SEC. The SEC seeks to administer and enforce legal obligations on private fund advisers through an active examination and oversight program, including with an announced focus on conflicts. Insurance companies advised by private fund advisers receive the benefits of this regulatory oversight.

The Task Force's considerations enunciate potential concerns that activities by private equity firms may present additional conflicts of interest in the context of their insurance-related activities. We believe that insurance regulators already have existing robust regulatory tools available to protect insurance companies, including capital requirements and ongoing examination and supervision. We welcome appropriate study and oversight and believe that regulators will find that the business practices identified, when properly executed, are not per se problematic for any insurance entity (including those affiliated with private equity) and should not be approached with a presumption of heightened risk. We also believe that the most productive areas of study will be on the activities at issue rather than the identity of the owner.

[4] *Global Private Equity & Venture Capital* Report (Prequin, 2021) available at https://www.preqin.com/insights/global-reports/2021-preqin-global-private-equity-and-venture-capital-report.

[5] National Association of State Retirement Administrators, "NASRA Issue Brief: Public Pension Plan Investment Return Assumptions," 2015, updated February 2017; Hamilton Lane data via Morgan Stanley Research, *"How Long Will the Golden Age of Private Markets Last?"* February 2021.

Again, the AIC commends the NAIC and the Task Force for seeking to further understand the relationships between Alternative Asset Managers and insurance companies. We stand ready to assist in this regard and would be pleased to answer any questions that you might have concerning the issues expressed in this letter.

Respectfully submitted,

Jason Mulvihill
Chief Operating Officer & General Counsel
American Investment Council