

Memo

To: Jon Godfread, Chair of the Risk-Based Capital Model Governance (EX) Task Force

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Subject: RRC Comments regarding Request for comments on *RBC Gaps*

Background

The Risk-Based Capital Model Governance (EX) Task Force exposed a new document on February 10, 2026, requesting comments "...from interested parties to identify gaps and inconsistencies across the RBC framework".

Risk & Regulatory Consulting, LLC ("RRC") regularly supports regulators in assessing the financial solvency of insurance companies, in the context of risk-focused examinations and financial analysis. As such, we have a perspective on the key risks currently facing insurance companies and the importance of the risk-based capital framework as a valuable tool to regulators.

We appreciate the continuing work that the RBC Model Governance Task Force has undertaken to modernize the RBC governance framework.

RRC appreciates the opportunity to offer our comments on this important issue. Should you have any questions, we would be glad to discuss our comments with you and Task Force members. Our comments will focus on the following areas:

- I. General Comments
- II. RBC for Property and Casualty
- III. RBC for Life
- IV. RBC for Health
- V. Investment issues related to RBC

Our comments on gaps represent areas for which we have general awareness based on our normal course of business, and are not meant to represent a comprehensive gap analysis. We realize that many of the items mentioned below may be currently under consideration by the Task Force for changes and updates.

I. General Comments

1. Many components of the RBC formulas were originally developed based on data from the 1970s–1980s. Since that time, there have been significant changes in markets, interest rates, mortality, longevity, and product design. Therefore, updates to certain components may be warranted.
2. Certain risk factors are treated inconsistently across lines of business. For example, Life RBC differs materially from P&C and Health formulas in structure, factor calibration, and accounting bases (e.g., amortized cost vs. market value). While some differences are needed based on the underlying risk profiles, some of these inconsistencies may create distortions when trying to assess weak capitalization for different types of insurers. The reasons for differences should also be well documented so that they are understood in the future.

II. RBC for Property and Casualty

1. The capital charges for lines of business that are subject to significant volatility or significant tail risk (i.e. very high expectation of loss in extreme scenarios) may be insufficient based on the current level of granularity in the RBC formula. For example, the blended personal auto liability reserve risk charge is likely to be insufficient for an insurer that has significant Personal Injury Protection exposure. Other Liability reserve risk charges are likely to be insufficient for insurers with significant mass tort exposure.
2. Smaller companies tend to have increased underwriting risk due to the volatility of their business; differences in volatility based on company size are not contemplated in the RBC formula.
3. Long-tailed lines' experience development could include more than the ten years captured in Schedule P (the data the RBC underwriting risk factors are calibrated on) to better capture the full development history for these lines.
4. The catastrophe risk adjustment does not address all catastrophe perils, for example Severe Convective Storms.

III. RBC for Life

1. Some risks are not directly reflected in the RBC formulas. For example, policyholder behavioral risks such as dynamic lapses, and product option utilization such as index-based account options in annuities and life insurance.
2. Interest rate risk (C-3) may be too simplistic for some annuity and life insurance products, such as Universal Life with Secondary Guarantees (ULSG), and other long-duration interest-sensitive products. For example, ULSG tail risk expands dramatically under prolonged low interest rate scenarios, a pattern not reflected in current factor-based C-3 formulas.
3. Interest rate risk (C-3 P1) factors, where RBC Cash Flow Testing is not required, assume well-matched asset/liability durations, adding only a fixed 50% load for mismatches. This simplification may understate or misstate real ALM risk, especially for products with embedded options or equity indexing. ALM mismatch may also be driven by movements in credit spreads, which is not directly contemplated.

4. The correlation formula may not adequately address observed risk correlations.

IV. RBC for Health

1. The Health RBC (H-RBC) factor-based approach does not sufficiently differentiate and account for risk across health products. For example:
 - a. ACA Risk-Adjustment (RA) Settlement Volatility & Timing Risk - Large, uncertain year-end RA receivables/payables (finalized mid-year following the coverage year) create material underwriting volatility that is not explicitly recognized in H-RBC. Current factors applied to premium/claims implicitly assume claim volatility but do not isolate RA transfer dispersion, which can swing margins materially especially for issuers with high concentration in a specific plan metal tier (e.g., Bronze, Silver, Gold, or Platinum) or plans that have narrow networks.
 - b. Rapid Enrollment Growth / Start-Up Expansion Risk - Rapid growth (e.g., new market entries, large group wins, or Medicaid auto-assignment) elevates pricing error and execution risk before credible experience emerges; current H-RBC does not include an explicit growth charge.
 - c. Catastrophic High-Cost Claim Concentration (Specialty/Gene Therapies) - A small number of ultra-high-cost therapies can create idiosyncratic tail risk in smaller or concentrated blocks even when average claim volatility is modest; existing H2 factors do not explicitly recognize claim concentration at the member-or-therapy level.
 - d. The Managed Care Credit categories may not be sufficiently detailed and appropriate as there has been an increase in managed care arrangements compared to when HRBC was developed where fee-for-service arrangements were dominant.
2. There may be inconsistencies regarding the application of the RBC formulas within Health and across other lines. For example:
 - a. Reinsurance - Credit-risk factors in Health RBC do not explicitly differentiate offshore or concentrated reinsurance counterparties for stop-loss/quota-share used by commercial and Medicaid issuers, whereas other lines have highlighted this exposure.
 - b. ASO - Administrative services-only (ASO) business has limited premium as an exposure base, yet embedded stop-loss or guarantees create underwriting-like volatility not commensurate with fee revenue used in H2.
 - c. Correlated Risks - Health insurers can experience correlated stresses (e.g., rapid growth + pricing shortfall + ACA RA swing). The current square-root covariance can over-diversify these risks.

V. Investment issues related to RBC

1. There are differences in treatment of asset risks across the three formulae, for example the Life RBC formula has risk category rankings for Commercial Mortgage Loans, while the formulas for other lines do not. The Life RBC formula has a beta adjustment for common stock, while the formulas for other lines do not. The Life RBC

formula has more granularity for Schedule BA than the formulas for other lines.

2. There is insufficient recognition of the risks that may arise associated with illiquid instruments. Because illiquidity can result in market value losses upon forced sales, the use of illiquid assets does have capital implications.
3. For fixed income instruments, there is insufficient recognition of differences in interest rate and spread duration that may also significantly contribute to market volatility.
4. There is insufficient recognition of the risk associated with Investments reported on Schedule BA that may be subject to high risk of volatility or payment uncertainty, which also may be difficult to assess given the lack of transparency for those assets.

Thank you for the opportunity to provide comments on this important topic. We can be reached at lynn.manchester@riskreg.com if you or other members have any questions.