

How Rated Note Feeders Help Insurers Tap Private Credit

By **Richard Shamos and Sarah Milam** (July 9, 2026)

Over the past decade, life and annuity companies have invested heavily in the private credit market, with insurer investments now comprising almost \$1 trillion of the private credit market's \$3 trillion in assets.[1]

This insurer participation in the credit market has driven product innovation through rated note feeders, with recent estimates of privately rated debt held by insurers at \$419 billion.[2]

Alongside this expansion, regulators have increased their scrutiny of such structured investment vehicles due to the potential risks they may pose to insurer solvency and the broader market. Yet despite this increased scrutiny, rated note feeders have shown a strength in product structuring that enables sponsors and insurance investors to balance the risks of private credit investment with the benefits of a rated debt investment.

Rated note feeder anatomy provides increased efficiency for insurance investment in private credit.

Rated note feeders are structured finance vehicles typically formed as partnerships or limited liability companies that invest all of their assets into an underlying private investment fund.[3]

These vehicles have proliferated in private credit markets due to their ability to issue rated debt, which provides a number of potential benefits to investors, including improved risk-based capital treatment for insurance company investors.

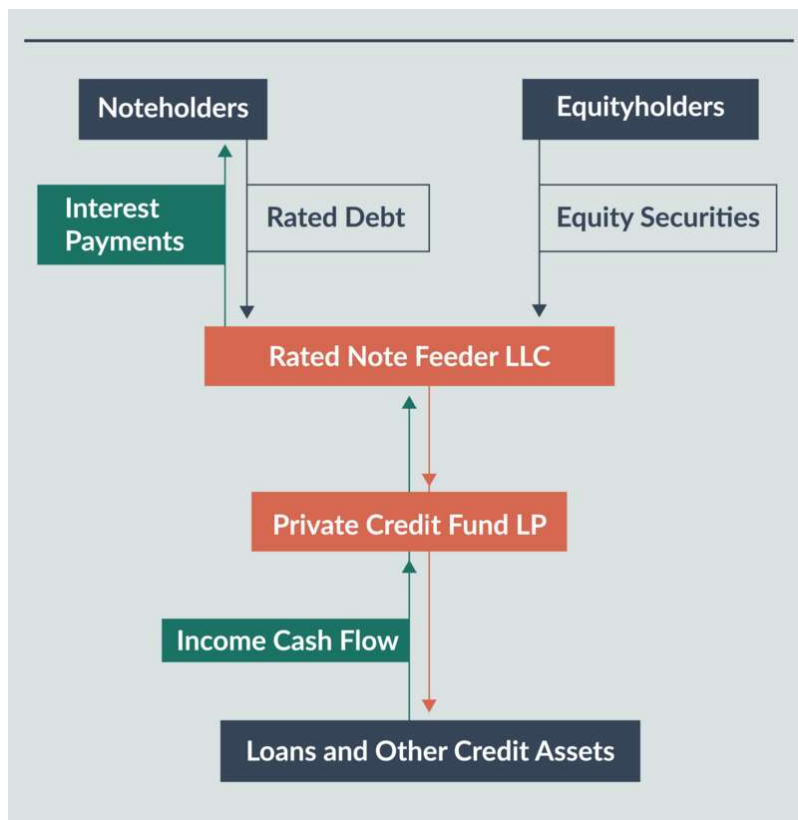
Unlike a standard feeder fund, a rated note feeder issues both debt and equity securities to its investors, then utilizes the cash flow on the underlying fund's investment portfolio to service interest payments on the debt. The debt is typically issued in multiple tranches, which are rated by a ratings agency and secured by the underlying fund interests, while the equity portion remains unsecured.



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Insurance investors will often invest in the entire "vertical strip" of capital issued by a rated note feeder, though horizontal structures where investors may pick and choose to only invest in the rated debt are becoming increasingly common.

Because the rated feeder's debt securities are secured by the underlying fund interests, a bank is often appointed to serve as collateral agent for the structure, and the documentation governing the rated note feeder's debt — typically a note purchase agreement or an indenture — includes governance provisions designed to manage noteholder rights.

When the underlying loans held by the fund are repaid or refinanced, the proceeds are returned to the rated note feeder and used to pay down the unpaid principal and interest on the investors' notes, with the remainder distributed to the equityholders.

These distributions are governed by a priority of payments waterfall, which details the manner and priority in which investment proceeds are applied toward accrued interest, deferred interest, principal and equity, among other items.

By investing in a private credit fund through a rated note feeder, insurance investors hold a mixture of investment grade debt, noninvestment grade debt and equity securities, rather than a 100% unsecured equity interest in a private credit fund.

Since insurers are required to set aside capital to offset the risk incurred in their investment portfolios, this basket of securities may provide a materially better return profile than a direct investment in the underlying fund.

Notably, the risk-based capital charge applicable to an insurer's holdings of investment grade debt is generally under 2%, and noninvestment grade debt (not including junk bonds) is generally under 10%, while the RBC for an equity interest in a private fund is 30%.^[4]

As a result, insurance investors that invest in a rated note feeder rather than a private credit fund directly can dramatically reduce the amount of risk-based capital they are required to set aside in connection with the investment and thereby increase their effective returns.

Ratings agencies play a central role in the issuance of such debt by rated note feeders by assessing the character and risk profile of the debt, which drives the attendant RBC for insurance investors. This gatekeeper function involves a review of a number of substantive factors, including the composition of a rated note feeder's capital stack, its priority of payments waterfall, the terms governing its security interest in the fund interests, and the character of the underlying portfolio of loans expected to be held by the fund.

Regulatory scrutiny of the industry provides a backdrop.

While rated note feeders represent an innovation in product structuring, their potential for abuse has not gone without notice by insurance and securities regulators, including the National Association of Insurance Commissioners and the U.S. Securities and Exchange Commission.

Notably, the NAIC has been particularly concerned that rated note feeders and similar vehicles may be used to repackage equity-like exposure without providing meaningful risk mitigation.

These concerns were a driving consideration behind the NAIC's adoption of a principles-based bond definition, which requires investors to assess the substantive characteristics of an investment and not merely its legal form when determining its risk-based classification.[5] Key substantive characteristics include the nature of the lending relationship, the existence (or absence) of credit enhancements, such as the use of a first-loss tranche or the collateralization or guarantee of securities, and the relationship between an instrument and the underlying cash flows supporting the return.[6]

In addition to this scrutiny from insurance regulators, the SEC, which oversees the registration of ratings agencies,[7] has increased enforcement of policies and procedures designed to handle conflicts of interests.[8] This includes an increased focus by the SEC on the use of private ratings, which are frequently deployed by rated-note feeders.[9]

Notably, the SEC has focused on potential conflicts with private ratings, noting that such ratings could foster so-called rating shopping and lead to a "race-to-the-bottom" in standards among ratings agencies.[10] As private credit markets continue to develop rated products and attract institutional capital, the SEC is likely to continue to examine the practices and procedures of market participants in launching rated credit products.

Rated note feeder flexibility facilitates the alignment of key features of debt securities and private credit funds.

Despite an increase in regulatory scrutiny, rated note feeders present a compelling structural solution for insurance investors by aligning the financing features of debt securities with the economic profile of a private fund in order to satisfy the substantive requirements for a rated debt issuance.

This economic alignment involves both qualitative and substantive components, including the coordination of back-end liquidity, front-end financing and key governance provisions.

Among the key differences between debt securities and private fund interests is the manner in which such instruments return capital to investors.

Notably, debt securities make fixed periodic payments of interest with a principal repayment due at maturity, while fund interests provide a sponsor with fiduciary discretion to make distributions and dispose of assets prior to expiration of the fund's term. This difference in liquidity can result in a duration mismatch and lead to heightened credit risk for the rated debt securities, with a corresponding drop in ratings.

However, by aligning the maturity of a rated debt instrument, often beyond 10 years, with the expected holding period of the illiquid credit assets held by a private credit fund, rated note feeders coordinate the duration of the rated debt securities with the term of the underlying fund and the liquidity of its assets.

This facilitates the repayment of rated debt principal in a manner that avoids putting additional stress on the fund's liquidation timeline or risking a fire-sale of assets.

In addition, rated note feeders partition the cash flow from the private loans held by an underlying fund into subordinated tranches of debt and equity securities designed to absorb the volatility of the underlying investment portfolio and reduce default risk. This vertical structuring provides additional risk mitigation and enables feeder sponsors to issue debt securities that are eligible for private credit ratings.

In addition to managing the back-end liquidity of funds, rated note feeders provide the structural flexibility to navigate the differing front-end drawdown and funding timelines of private funds and debt securities.

Notably, drawdown funds typically require an upfront commitment that can be drawn down over the entirety of the fund's investment period, generally three to five years, and even thereafter. Debt investors, on the other hand, typically want to deploy their capital quickly, generally not beyond two years. This mismatch can expose the feeder to the risk of having to make a fund capital contribution at a point in time when its investors are no longer required to make corresponding fundings.

In addition, rated feeder debt securities are generally delayed draw obligations, not revolvers, and so cannot be redrawn or recycled once they have been invested, while closed-end funds often permit recycling during the fund's investment period — and open-end funds engage in perpetual recycling.

As a result, the available undrawn capital at a rated note feeder may be depleted at a faster rate than the available capital of the underlying fund without the prospect of being redrawn, exposing the feeder to potential default risk.

While this difference represents a fundamental mismatch between the funding mechanics of debt securities and private funds, sponsors can mitigate the effects of this divergence through deliberate planning around drawdown timelines and recycling terms at the fund and rated note feeder levels. Effective management of these funding obligations is a key consideration in credit risk modeling that drives ratings decisions in debt issuances.

Finally, debt investors and fund investors generally have different risk profiles, which can give rise to conflicts of interest that vary depending on whether the rated note feeder is structured as a vertical or horizontal issuance.

In a vertical structure, the capital stack is "stapled," such that all investors must buy the full strip of senior debt, mezzanine debt and equity offered by the issuer, and therefore generally hold a basket of securities that follows the overall risk and return profile of the underlying private fund.

In a horizontal structure, on the other hand, investors can pick and choose which instruments they want to invest in, and so may have materially different risk and return profiles than direct fund investors.

This can drive divergent and at times competing terms at the fund, feeder and investor level. For example, fund level defaults can trigger cramdowns and forced sales of fund interests, which is generally an accepted remedy among private fund investors.

However, the potential loss of collateral securing a debt investment would be intolerable to secured lenders and could be fatal to the rating of a private debt security. By layering a second level of governance at the feeder level, rated note feeders can reconcile key default terms and ensure that remedies are exercised in a manner that upholds the essential financial features of each structure.

This ability to reconcile key terms is central to the ratings process and the issuance of rated debt, which ultimately drives the improved investment outcome for insurance investors.

Concluding Thoughts

Despite divergences in the economic and structural features of rated debt and private credit funds, through a diverse capital stack and customizable features, rated note feeders provide the flexibility to align the key terms of debt securities with the underlying terms and features of private credit funds.

While the growth of the market for rated note feeders and similar structures has faced both product and regulatory challenges, the market opportunity for investors in private credit products remains robust.

For insurers, rated note feeders offer a compelling way to access private credit yields through debt instruments by balancing key features of debt investment with the structural and economic profiles of private credit funds.

In particular, rated note feeders should be crafted to align a fund's cash flows with the economic and regulatory demands of an interest-bearing rated note structure. Provided they are structured accordingly, rated note feeders present sponsors with an enhanced ability to attract insurance capital in income-producing credit strategies and to provide an efficient capital solution to insurance investors' needs.

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[1] Gillers, Heather. Insurers' \$1 Trillion Buildup in Private Credit Is Leaving Regulators in the Dust, Wall St. J. (April 7, 2026), available at: <https://www.wsj.com/finance/regulation/insurers-1-trillion-buildup-in-private-credit-is-leaving-regulators-in-the-dust-5f84cad8>. See also, Morgan Stanley. Understanding Private Credit's Rapid Growth (October 3, 2025), available at: <https://www.morganstanley.com/ideas/private-credit-outlook-considerations>.

[2] Id.

[3] Due to the need for consistent periodic income to finance the notes issued by the rated note feeder, such products have proliferated in income-generating asset classes like private credit.

[4] MetLife Investment Management. A Very Long Engagement: Asset Allocation Implications of U.S. Life Insurance Risk-Based Capital Charges (August 5, 2021), available at: <https://investments.metlife.com/content/dam/metlifecom/us/investments/insights/research-topics/Insurance-am/a-very-long-engagement/MIM-A-Very-Long-Engagement-Asset-Allocation-Implications-of-US-Life-Insurance-Risk-Based-Capital-Changes.pdf>.

[5] Recamara, Josh. NAIC tightens grip on insurers' investment risk with bond and CLO overhaul, Ins. Bus. Mag. (April 20, 2026), available at: <https://www.insurancebusinessmag.com/us/news/claims/naic-tightens-grip-on-insurers-investment-risk-with-bond-and-clo-overhaul-572390.aspx>.

[6] NAIC. Principles-Based Bond Definition, Statutory Issue Paper No. 169, available at: https://content.naic.org/sites/default/files/inline-files/Bond%20IP%20-%20Adopted%202024%20Summer_0.pdf.

[7] See, Section 15E of the Securities Exchange Act of 1934, as amended (15 U.S. Code §170-7) and Rule 17g-5 under the Exchange Act regulations (17 CFR §17g-5).

[8] See, Nationally Recognized Statistical Rating Organizations, Release No. 34-72936 (Aug. 27, 2014), 79 FR 55078, 55220-22 (Sept. 15, 2014) (2014 Adopting Release), available at: <https://www.sec.gov/files/2025-ocr-staff-report-compliant-4-24-26.pdf>. (Notably, in the SEC's Staff Report (infra note 10), the SEC emphasized that, "under Rule 17g-5(c)(8), an NRSRO is prohibited from issuing or maintaining a credit rating where a person within the NRSRO who participates in determining or monitoring the rating, or developing or approving procedures or methodologies used for determining the rating, also (i) participates in sales or marketing activities of the NRSRO or its affiliate, or (ii) is influenced by sales or marketing considerations.")

[9] In 2022, the SEC charged an NRSRO of violating conflict of interest rules by having allowed business and sales considerations to drive ratings decisions and by failing to establish policies and procedures designed to effectively prevent such conflicts. (See, U.S. Securities and Exchange Commission. SEC Charges Egan-Jones Ratings Co. and CEO with Conflict of Interest Violations, 2022-111(June 21, 2022), available at: <https://www.sec.gov/newsroom/press-releases/2022-111.>)

[10] U.S. Securities and Exchange Commission. Staff Report on Nationally Recognized Statistical Rating Organizations (April 2026) ("Staff Report"), available at: <https://www.sec.gov/files/2025-ocr-staff-report-compliant-4-24-26.pdf>.