AVANTE CAPITAL PARTNERS

AVANTE PERSPECTIVES · STRUCTURAL GUIDE

Rated Insurance Feeder Structures: How a Rated Note Wraps an Unrated Fund

For institutional allocations evaluating Rated Note Structures: how a rated feeder converts fund exposure into an insurance-eligible instrument.

The Question Being Asked

An insurance company allocator considering a private credit or private equity fund is not only asking whether the fund is a good investment. It is asking whether the exposure can sit on its balance sheet in a form its regulator and its internal capital model will accept. Insurance capital regimes reward assets that carry a credit rating and penalize, through higher capital charges, assets that do not. A rated insurance feeder structure exists to answer that specific balance sheet question without changing what the underlying fund actually does. This paper explains how such a structure works, where the rating comes from, what happens if the underlying investments underperform, and how it differs from investing in the fund directly.

This paper is descriptive, not promotional. It does not evaluate any manager's track record or make a case for allocating capital. It exists because a rated feeder, like an SBIC-leveraged structure, is unfamiliar enough that a committee should understand the mechanism before it discusses the specific terms of any offering.

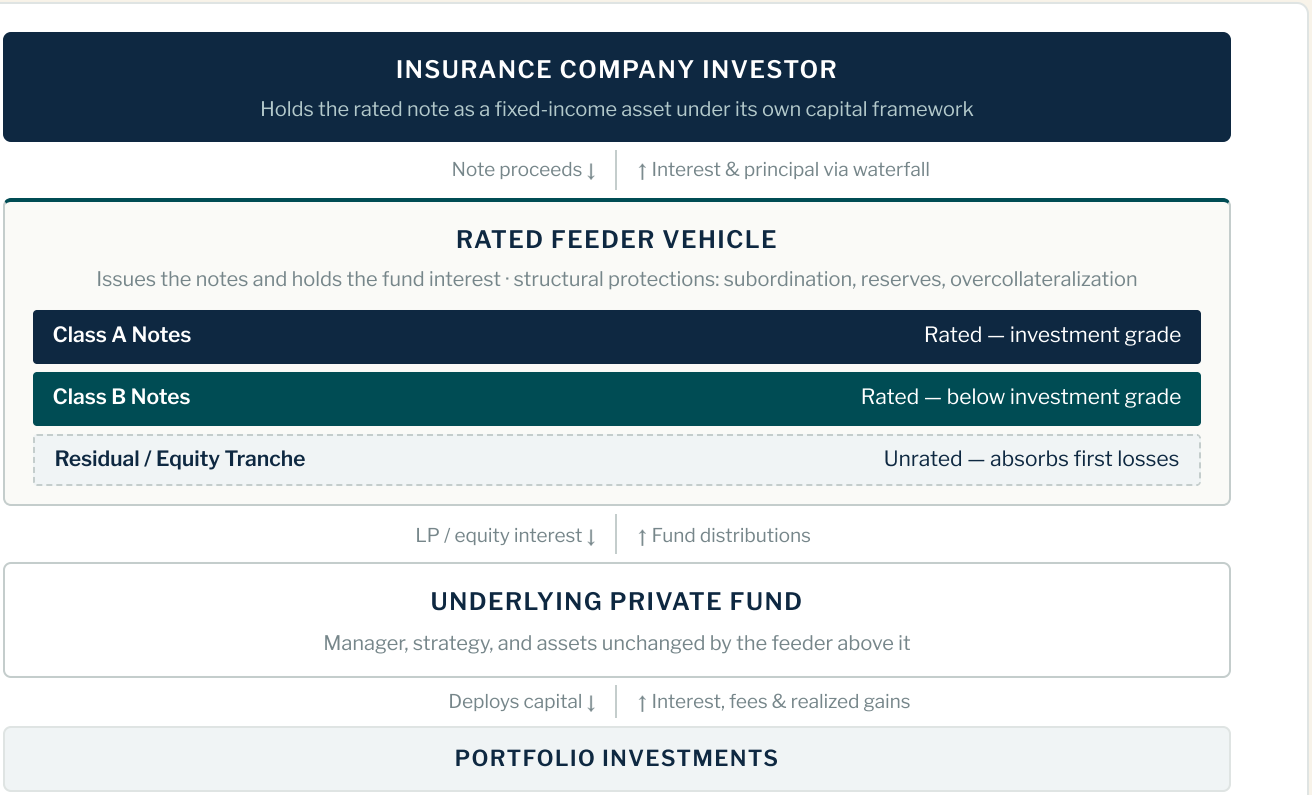
A note on scope: this paper describes the feeder form because it is the most common way rated note structures are presented to insurers. Avante's rated note vehicle is structured differently, as a parallel fund investing alongside the flagship fund rather than feeding into it; the mechanics below apply either way, and the distinction is addressed on the closing pages.

What a Rated Feeder Is Built To Do

A rated insurance feeder is a separate legal vehicle, typically structured as a note-issuing entity, interposed between an insurance company investor and an underlying private fund. The insurer buys a note issued by the feeder rather than a limited partnership interest in the fund itself. The feeder, in turn, invests the note proceeds into the fund as an equity or debt holder. A credit rating agency rates the note based on the credit characteristics of the fund's underlying portfolio and the structural protections built into the feeder, similar in concept to how a rating agency rates an asset-backed security.

The purpose of this arrangement is capital treatment, not return enhancement. A rated note held by an insurer can, under the insurer's applicable capital framework, receive a materially lower capital charge than the same economic exposure held as an unrated fund interest. Because insurance companies hold capital against every asset on their books, the capital charge directly affects the net return the insurer can achieve on a given allocation. The feeder does not change the underlying fund's investment strategy, its manager, or its assets. It changes the form in which the insurer holds the claim on those assets.

ILLUSTRATIVE RATED NOTE FEEDER STRUCTURE



Defined Terms Used in This Paper

Feeder Vehicle: The intermediate legal entity that issues rated notes to insurance investors and holds the corresponding investment in the underlying fund.

Rated Note: The debt instrument issued by the feeder vehicle, evaluated and assigned a credit rating by a nationally recognized statistical rating organization based on the underlying portfolio and structural protections.

Underlying Fund: The private credit or private equity fund in which the feeder invests, and which the manager actually operates day to day.

Waterfall: The contractual order in which cash generated by the underlying fund is applied, first to feeder expenses and note interest, then to principal, then to any residual equity holders of the feeder.

The Mechanism, Step by Step

1. THE UNDERLYING FUND IS FORMED AND CAPITALIZED FIRST

The manager forms and operates the underlying fund in the ordinary course, raising commitments from limited partners and deploying capital according to its stated strategy. The feeder structure is layered on top of, not instead of, this fund. Nothing about how the fund selects investments or manages its portfolio changes because a feeder exists above it.

2. THE FEEDER VEHICLE IS FORMED TO HOLD THE INSURER'S EXPOSURE

A separate entity is created specifically to interpose between the insurer and the fund. This entity has its own governing documents, its own cash flow waterfall, and its own set of structural protections, which may include subordination, overcollateralization, or reserve accounts, depending on how the specific feeder is designed. The feeder's assets consist primarily of its interest in the underlying fund, and its liabilities consist primarily of the notes issued to insurance investors.

3. A RATING AGENCY EVALUATES THE STRUCTURE

The rating agency reviews the underlying fund's portfolio characteristics, historical or projected cash flows, and the feeder's structural protections to determine what rating the note can support. This is analogous to how a rating agency evaluates a securitization backed by a pool of loans, though the specific methodology depends on the asset class and the rating agency involved. The rating attaches to the note, not to the fund and not to the manager.

4. THE INSURER PURCHASES THE RATED NOTE

The insurer holds the note as a fixed income or fixed-income-like asset rather than as a fund interest. This affects how the insurer classifies the asset for statutory accounting and regulatory capital purposes, which is the entire commercial reason the structure exists. The insurer's actual economic exposure still runs, indirectly, to the performance of the underlying fund's portfolio.

5. CASH FLOWS THROUGH THE WATERFALL

As the underlying fund generates interest income, fee income, or realized gains, cash moves up to the feeder and is applied according to the waterfall: feeder expenses and note interest first, then scheduled principal, then any residual amount to subordinated or equity holders of the feeder. The insurer, as note holder, sits at a defined position in this waterfall rather than sharing pro rata in fund distributions the way a direct limited partner would.

Confidential — Not for distribution

What Happens Under Stress

This is the section a committee most needs and the one most descriptions of rated feeders skip. The rated note is only as strong as two things: the performance of the underlying fund's portfolio, and the structural protections built into the feeder itself. If the underlying fund's portfolio underperforms, whether through defaults, markdowns, or slower-than-expected realizations, the effect on the note depends entirely on where subordination and reserves are sized relative to that underperformance.

IMPAIRMENT OF THE UNDERLYING PORTFOLIO

A material decline in the underlying fund's asset values does not automatically mean the rated note defaults. Structural protections such as subordinated tranches, reserve accounts, or overcollateralization are specifically designed to absorb a defined amount of underperformance before the rated note is affected. However, the specific loss coverage of any given feeder, meaning how much underlying portfolio impairment the note can absorb before its own payments are affected, is a function of that transaction's structural documents.

RATING MIGRATION

If the underlying portfolio's credit quality deteriorates, the rating agency can downgrade the note even before any payment default occurs, because the rating reflects forward-looking credit risk, not just current payment status. A downgrade can itself trigger consequences for the insurer, including a higher regulatory capital charge on the position and, depending on the insurer's own investment guidelines, a potential requirement to reduce or exit the position. This is a meaningful difference from a direct limited partnership interest, which is not subject to third-party rating migration in the same way, though it is separately subject to net asset value markdowns reported by the manager.

PRIORITY OF PAYMENT

Because the insurer holds a note rather than a direct fund interest, it occupies a defined seat in the feeder's waterfall rather than sharing losses pro rata with all fund investors. This can mean the note holder is better protected than a direct equity investor in the same underlying fund, if the note sits senior to other capital in the feeder. It can also mean the note holder has no claim on upside beyond its stated interest rate, since the note is a debt instrument with defined payment terms rather than a residual equity claim.

What This Paper Does Not Cover

This paper describes the mechanism in general terms. It does not cover the specific state insurance capital regulations, NAIC risk-based capital designation criteria, or the particular rating agency methodology that would govern the capital treatment or the default and remedy provisions of any specific rated feeder. Any committee evaluating a specific rated feeder proposal needs the actual rating agency presale report, the specific insurer's applicable statutory accounting and capital framework, and the feeder's governing and offering documents.

Confidential — Not for distribution

How This Differs From a Direct Fund Investment

An insurer that is already familiar with investing directly in private credit or private equity funds as a limited partner has a useful reference point for understanding what changes and what does not change in a rated feeder.

FEATURE	DIRECT LIMITED PARTNERSHIP INTEREST	RATED INSURANCE FEEDER NOTE
Legal claim held by insurer	Equity interest in the fund, sharing pro rata in gains and losses	Debt instrument issued by a separate feeder vehicle
Credit rating	None; evaluated internally by the insurer	Rated by a nationally recognized statistical rating organization
Position in cash flow priority	Pro rata with other limited partners, subject to the fund's own distribution waterfall	Defined seniority within the feeder's waterfall, which may be senior to other feeder capital
Exposure to underlying manager's strategy	Direct and full	Indirect, filtered through the feeder's structural protections
Effect of underlying portfolio underperformance	Flows through directly to the limited partner's capital account	Absorbed first by subordination or reserves, subject to the specific structure's loss coverage
Sensitivity to third-party rating migration	Not applicable	Note can be downgraded based on forward-looking credit assessment, independent of realized losses
Regulatory capital treatment for an insurer	Governed by the insurer's treatment of unrated fund interests	Governed by the insurer's treatment of rated debt instruments, generally more capital-efficient

Confidential — Not for distribution

Why an Insurer or Sponsor Considers This Structure at All

Insurance companies are not indifferent between two investments with identical expected returns if one requires materially more regulatory capital to hold. A rated feeder is a response to that constraint rather than an attempt to change the underlying investment's actual risk. For a sponsor or independent sponsor raising capital, understanding that an insurance allocator may need this wrapper is different from assuming the insurer wants different underlying assets. The economics the manager delivers at the fund level are the same regardless of whether a given investor accesses them directly or through a feeder.

Sponsors should also understand what the feeder does not do. It does not improve the underlying fund's actual credit quality, and it does not eliminate the risk that the underlying portfolio underperforms. It reallocates who bears the first losses, through subordination, and it changes how a specific class of regulated investor is permitted to hold and capitalize the resulting exposure. Those are structural and regulatory facts about the insurer's balance sheet, not statements about the fund's investment merit.

How Avante’s Structure Differs: A Parallel Fund, Not a Feeder

Avante’s rated note vehicle is organized as a parallel fund that invests alongside the flagship fund, rather than as a feeder that invests into it. The building blocks are the same: a note-issuing vehicle, rated notes held by insurance investors, a defined waterfall, and structural protections sized to support the rating. What changes is what the vehicle holds. A feeder holds a limited partnership interest in the underlying fund, so its noteholders’ claim runs through the fund’s own waterfall. A parallel rated fund holds its own interests in the same investments, side by side with the main fund, so the noteholders’ claim runs to assets the vehicle owns directly.

For an allocator, the practical differences favor directness: the rating analysis looks through to the vehicle’s own portfolio rather than to a fund interest, cash flows reach the waterfall without passing through a second fund’s distribution mechanics, and the vehicle’s governing documents, not another fund’s, define the noteholders’ rights. The diligence checklist in this paper applies unchanged; the answers simply come from the parallel fund’s own documents and portfolio.

What This Means for an Allocator

A rated insurance feeder is a wrapper, not a different investment strategy. The underlying fund's manager, portfolio, and strategy are unchanged by the existence of the feeder above it. What changes is the legal form of the claim, the presence of a third-party credit rating, the priority of payment in a defined waterfall, and the resulting regulatory capital treatment available to an insurance company holder. A committee evaluating a specific rated feeder proposal for the first time should request the rating agency's actual methodology and presale materials, the specific subordination and reserve mechanics of that transaction, and confirmation of how the insurer's own regulatory framework treats the resulting note, since none of those figures can be assumed or estimated in the abstract.

Key takeaways

- A rated insurance feeder is a separate legal vehicle interposed between an insurer and an underlying fund; it issues a rated note to the insurer while investing the proceeds into the fund, without changing the fund's own strategy or management.
- The credit rating attaches to the note and the feeder's structural protections, not to the underlying fund or its manager, and can migrate independently of the fund's realized performance.
- Underlying portfolio underperformance is absorbed first by the feeder's own subordination, reserves, or overcollateralization, meaning the note holder's actual loss exposure depends on that specific transaction's structural sizing, not on fund-level losses alone.
- Holding a rated note changes an insurer's position from a pro rata equity claim in the fund's waterfall to a defined-priority debt claim in the feeder's waterfall, which affects both loss absorption and regulatory capital treatment.
- This structure is a balance sheet and capital efficiency mechanism for the insurance holder, not a change to the underlying investment's actual credit quality or strategy.
- Avante's rated note vehicle is a parallel fund investing alongside the flagship fund rather than a feeder into it: the same mechanics, with the noteholders' claim running to assets the vehicle holds directly.

Please refer to Notices and Disclosures on the following page.

Notices and Disclosures

SOURCES AND REFERENCES

This paper describes rated feeder mechanics in general structural terms. It does not address state insurance capital regulations, NAIC risk-based capital designation criteria, or any specific rating agency methodology; a committee evaluating a specific rated feeder proposal should obtain the rating agency's presale and methodology materials, the applicable statutory accounting and capital framework, and the transaction's governing and offering documents. The structure diagram herein is illustrative only and is not representative of any actual fund, feeder, or portfolio; tranche count, ratings, and structural protections vary by transaction.

IMPORTANT DISCLOSURES

This document has been prepared by Avante Capital Partners for informational and discussion purposes only. It is descriptive, not promotional. It does not constitute an offer to sell or a solicitation of an offer to buy any security, and it does not constitute investment, legal, tax, or accounting advice. Recipients should consult their own advisors as to the matters described herein.

The information contained herein is based on regulatory and third-party source material believed to be reliable as of the date of this document, but its accuracy and completeness are not guaranteed, and it is subject to change without notice. Regulatory provisions summarized herein are simplified for discussion purposes; the governing regulations and program documents control in all cases.

Past performance is not indicative of future results, and all investments involve risk of loss, including loss of principal. Any historical performance data presented reflects the cited studies and data sets, not the performance of any Avante fund or any specific investment.

Certain statements herein reflect expectations regarding regulatory frameworks and market conditions and are subject to change. References to specific legislation and regulations reflect the authors' understanding as of the date of this document.

This document is confidential and intended solely for the recipient to whom it is delivered. It may not be reproduced or distributed, in whole or in part, without the prior written consent of Avante Capital Partners.