OFFICE OF
GENERAL
COUNSEL

THE AUTO CLUB GROUP
1 AUTO CLUB DRIVE,
DEARBORN. MICHIGAN 48126

JOHN BRUNO, ESQUIRE
VICE PRESIDENT, SECRETARY GENERAL COUNSEL
TELEPHONE (313) 336-1795
FACSIMILE: (313) 336-1246

September 16,2016

Mr. Robert deV. Frierson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave, N.W.
Washington, D.C. 20551

RE: Docket No. R-1539 Advance Notice of Proposed Rulemaking "Capital Requirements for Supervised Institutions Significantly Engaged in Insurance."

Dear Sir:

The Auto Club Group ("ACG"), Auto Club Services, Inc. ("ACS") and Auto Club Insurance Association ("ACIA"), each a grandfathered unitary savings and loan holding company ("SLHC"), appreciate the opportunity to submit these comments on the Advance Notice of Proposed Rulemaking on "Capital Requirements for Supervised Institutions Significantly Engaged in Insurance Activities" published by the Board of Governors of the Federal Reserve System ("FRB") on June 14, 2016 (81 Fed. Reg. 38631) (the "ANPR").

The Auto Club Group, Auto Club Services, Inc. and Auto Club Insurance Association

The Auto Club Group is a member of the federation of automobile clubs doing business under the American Automobile Association ("AAA") banner. Established in the early 1900's, ACG provides roadside emergency, travel and other automotive services to its members. Auto Club Services, Inc. is a wholly-owned subsidiary of ACG and is the management company for the enterprise, and the attorney-in-fact for ACIA. Auto Club Insurance Association and its property and casualty subsidiaries primarily underwrite automobile and homeowners' insurance products. ACIA also provides life insurance through one of its subsidiaries. For purposes of regulation by the FRB, ACG is considered the top-tier holding company, although ACIA is the primary operating entity within the consolidated group. By virtue of their ownership and control of Auto Club Trust, FSB, ("ACT") each of ACG, ACS and ACIA is a registered savings and loan holding company pursuant to Section 10 of the Home Owners' Loan Act of 1933 ("HOLA"). Each company is qualified as a grandfathered unitary SLHC under Section 10(c)(9)(C) of the HOLA. As of December 31, 2015, ACG (including ACS) had consolidated GAAP assets of $1.2 billion. ACIA had combined assets under statutory accounting principles of S4.2 billion. The financial statements of ACG and ACIA are not consolidated pursuant to recent FASB guidance on variable interests in a legal entity.

Overview of the ANPR

ACG, ACS and ACIA support the fundamental framework set forth in the ANPR to establish capital requirements for holding companies engaged significantly in insurance activities. We agree that capital is an important safeguard to protect the safety and soundness of financial institutions; enhance the resilience of financial institutions to position them better to navigate periods of financial or economic stress; and to mitigate certain threats to financial stability. We appreciate the FRB's recognition of the differences in banking and insurance entities and the complementary, yet different, objectives of the agencies that supervise these entities. In this regard, it is important to continue to recognize key differences in risks posed by banking and insurance companies as the FRB develops and finalizes its capital regulation. Unlike credit, liquidity and interest rate risk, the primary risks associated with banking, a property and casualty insurance company must assess the probability of future loss through a series of actuarial models, many of which are local rather than national in scope. As a result, the capital needs of an insurance company are generally far different from those of a banking company.

Similar to the differences in risks and capital needs, the regulatory schemes for banking and insurance companies are very different. The insurance industry has developed under a coordinated state scheme, pursuant to which state regulators govern the insurance industry, but act in many instances in a coordinated manner through the National Association of Insurance Commissioners ("NAIC"). The state regulatory scheme developed by state regulators to address the capital requirements of insurance companies has been quite effective in maintaining the integrity of the insurance industry in the same manner that the capital requirements developed by the bank regulatory agcncies have been effective in addressing the safety and soundness of ID Is. Congress has long recognized and supported the state regulatory structure for insurance, most recently with the passage of S. 2270 in 2014 which clarified that the FRB may apply insurance-based capital standards to the insurance portion of any insurance holding company it oversees.

As stated above, we support the general framework outlined by the ANPR as it relates to less complex insurance depository holding companies: an insured depository institution will continue to meet capital requirements of its primary federal regulator (which in the case of ACT is the OCC); companies that are primarily engaged in insurance will meet the requirements of the state insurance regulatory authority; and a building block approach ("BBA") will be used to determine the aggregate capital required of the entire enterprise. Our primary concern relates to the capital requirements that will be imposed on the nonbanking, noninsurance companies that are part of the organization. Currently, the ANPR contemplates that those affiliates that are neither banking nor insurance companies must meet the capital requirements of the FRB's Regulation Q. Our concerns on this issue and comments on the other aspects of the ANPR are set forth below.

Comments on the ANPR

Appropriate Capital Framework. We believe that the FRB has captured the appropriate risks associated with insurance depository holding companies ("IDHC"). Further, we believe that the same capital framework should apply to all IDHCs in order to ensure consistency of regulation, supervision and oversight. With respect to the definition of "significantly engaged in insurance," we would prefer that a percentage of revenues test be utilized rather than the proposed 25% of combined assets test to determine whether a holding company qualifies for IDHC treatment.

The Building Block Approach. We agree with utilizing the BBA for IDHCs. As we understand it, the BBA will utilize an "aggregate approach" whereby the capital requirement for the entire organization will be the sum of the capital requirements for each component company. That is, under the BBA, the capital requirement for the entire organization would be the sum of the capital requirements for all insurance companies under state insurance regulations, the capital requirement for the insured depository institution under applicable banking regulations and the capital requirements that may be imposed on nonbanking, noninsurance companies ("unregulated entities").

In applying the BBA, it is critical that an aggregate approach is utilized, particularly for companies that may have one or more unregulated entities. In this regard, it is important to note that the capital needs of unregulated commercial entities are far different than the needs of banking or insurance entities. Unlike banking or insurance entities that need capital to protect against future losses, a commercial entity utilizes capital to fund future growth and expansion of the business. Excess capital penalizes a commercial enterprise as capital should be put to use in the business or returned to the equity owners. For this reason, most companies including ACG may opt to keep the capital levels of certain commercial subsidiaries at a minimum and draw on the financial resources of the parent when capital is needed. An aggregate approach to the BBA would ensure that the entire organization is not penalized by the capital position of an unregulated entity so long as the entire organization meets the combined capital requirements of all entities within the group.

In addition, the BBA should be clarified to provide that all companies within the combined statutory accounting financial statements of the top tier or consolidating insurance company are governed by the state insurance capital requirements. In certain instances, subsidiaries of insurance companies are combined with the parent utilizing the equity method of accounting. The equity of these companies is included in the parent's balance sheet when determining compliance with state insurance capital regulations. We believe that no individual capital requirements should be imposed on such subsidiaries so long as the parent insurance company meets its capital requirements.

Advantages and Disadvantages of the BBA. We agree with the ANPR that the BBA presents significant advantages, including: efficient use of existing regulatory capital frameworks; ease of implementation; relatively low additional regulatory costs and burdens; and capital requirements that are tailored to the risks of distinct jurisdictions. We also agree that the BBA presents some weaknesses, but we believe that such weaknesses are manageable. For instance, although the BBA utilizes an aggregate approach (each company's individual capital requirements are added to determine the total enterprise capital requirement) rather than a consolidated approach, the aggregate approach more appropriately takes into consideration the differences between banking and insurance capital needs and capital solvency frameworks, but also better recognizes differences in local factors that impact insurance and are taken into account by state insurance regulatory authorities.

The BBA does not increase the risk of regulatory arbitrage as all insurance companies currently are subject to capital adequacy requirements at the state level. A weakened insurance company will find little opportunity to seek a more "lenient" regulator if the real or perceived purpose of re-domestication is to reduce capital requirements. Additional legal-entity level stress tests would not be required for banking and insurance companies within the group, as such entities are presently subject to stress test requirements based on the size of the institution.

Recordkeeping and Data Requirements. The BBA allows the FRB to ensure the capital adequacy of IDHCs while recognizing the state supervisory framework that has been implemented successfully by insurance regulators. We do not believe that any additional records, data requirements or systems would be necessary to implement the BBA, as IDHCs would be able to utilize current information already supplied to state insurance regulators. With respect to ACIA, the company produces financial statements under statutory accounting principles ("SAP") for itself as well as its insurance subsidiaries. These financial statements are utilized by the insurance regulators to test against insurance capital and reserve requirements. Consequently, there would not be any difficulty in utilizing the financial statements of an IDHC for purposes of the BBA.

Scalars. Regarding the use of scalars, we do not believe that different levels of capital should be required for different domestic regulatory authorities, provided that the state insurance department has been accredited by the NAIC. The NAIC's mission is to create a system of effective solvency regulation by requiring each member insurance regulatory agency to have adequate statutory and administrative authority to regulate an insurer's corporate and financial affairs. The NAIC's mission to ensure effective solvency regulation is consistent with the FRB's mission to ensure the strength of financial institution holding companies. As a result, we believe that the capital requirements of a state regulatory authority, whose operations and legal authority meet the requirements of the NAIC, should not be subject to scalars. Further, we believe that the use of scalars for domestic, NAIC accredited state regulatory authorities may result in regulatory arbitrage, as insurance companies may be encouraged to choose a state of domestication based primarily on capital requirements. Scalars would also damage the reputation of a state authority and the reputations of those regulated insurance companies that are subject a scalar, as a scalar would imply that the regulatory authority and the regulated insurance companies are somehow weaker than those authorities or companies that are not subject to, or subject to a lower, scalar. Again, our view is that if a state regulatory authority is accredited by the NAIC, then the capital requirements of that authority, as interpreted and implemented by that authority, should be used without a scalar by the FRB for IDHCs.

Baseline Capital Requirements and State Regulation Variances.

In applying the baseline capital requirement for insurance entities, the Company Action Level is the most appropriate to establish a minimum level of capital. Under the NAIC Model Act, the Company Action Level is defined as twice the Authorized Control Level RBC. A company that does not meet this level of capital (a "Company Action Level Event") is required to undertake the following series of actions:

(1) Identify the conditions which contribute to the Company Action Level Event;

(2) Propose corrective actions which the insurer intends to take and would be expected to result in the elimination of the Company Action Level Event;

(3) Provide projections of the insurer's financial results in the current year and at least the four (4) succeeding years, both in the absence of proposed corrective actions and giving effect to the proposed corrective actions, including projections of statutory operating income, net income, capital and surplus;

(4) Identify the key assumptions impacting the insurer's projections and the sensitivity of the projections to the assumptions; and

(5) Identify the quality of, and problems associated with, the insurer's business, including but not limited to its assets, anticipated business growth and associated surplus strain, extraordinary exposure to risk, mix of business and use of reinsurance, if any, in each case.

Under the NAIC Model Act, an insurer whose capital continues to decline will become subject to increasingly more stringent regulatory actions, including placing the insurer under the control of the insurance regulatory authority. These mandated actions, which increase in severity as capital declines, are similar to the prompt corrective action regulations applicable to banking institutions.

We do not believe it is necessary to make adjustments based on state variances to accounting standards. Insurance is, by nature, a local product with significant variances among the states on the amount of coverage an insurance company is required to offer customers. Unlike a home or auto loan that is virtually a homogeneous product nationwide, each state imposes different terms, deductibles, and minimum and maximum coverage limits on insurance products. To this end, each state regulatory authority has formulated solvency requirements, and accounting rules that are consistent with such solvency requirements, that are tailored to meet the specific insurance laws of each state. The state solvency scheme, as supported by state approved accounting rules, has proven very effective in ensuring the viability of the insurance industry. For these reasons.

we do not believe that the FRB's capital rule should be adjusted for any state approved accounting variances.

Unregulated Entities. Regarding unregulated entities, the ANPR proposes that these companies would be subject to the FRB's Regulation Q. We believe that additional research and field testing is required before Regulation Q can be applied to such entities. For instance, additional research should be performed to determine how the risk weightings would be applied to such entities. The balance sheets of these entities may include such assets as inventory, real estate and receivables that pose far different risks for an unregulated entity than such assets would pose to a financial institution. Additionally, many unregulated entities carry goodwill on their books. Under Regulation Q, goodwill and intangible assets are deducted from capital. We agree that tangible capital provides the best protection from future loan losses and rightfully should be deducted from bank capital. However, commercial entities do not retain capital to protect against future losses, but rather to grow the business. Goodwill, often created in connection with the acquisition of a business, represents the brand of the acquired company, which may have a tangible value apart from its assets and liabilities. Goodwill and intangible assets do not have the same impact on the financial condition of a commercial entity as compared to a bank. For this reason, we suggest, that unregulated commercial entities not be required to deduct the value of goodwill and intangible assets from capital in determining aggregate enterprise capital.

* * *

The Auto Club Group, Auto Club Services, Inc. and Auto Club Insurance Association very much appreciate the FRB's consideration of the comments and would be pleased to answer any questions the FRB or the staff might have.

Very truly yours,

John Bruno
Vice President, Sccrctary and General Counsel