USAA®
9800 Fredericksburg Road
San Antonio, Texas 78288

August 5, 2011

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
regs.comments@federalreserve.gov

Re: Proposed Rule on Capital Plans (Regulation Y; Docket No. R-1425; RIN 7100-AD 77)

Dear Ms. Johnson:

United Services Automobile Association (USAA) is pleased to provide our comments with respect to the Board of Governors of the Federal Reserve System (the Board) Proposed Rule on Capital Plans[1] (the Proposed Rule).

USAA is a membership-based association, which together with its family of companies, serves present and former commissioned and noncommissioned officers, enlisted personnel, retired military, and their families. Since USAA's inception in 1922 by a group of U.S. Army officers, we have pursued a mission of facilitating the financial security of our members and their families by providing a full range of highly competitive financial products and services, including personal lines of insurance, retail banking and investment products. Our core values of service, honesty, loyalty and integrity have enabled us to perform consistently and be a source of stability for our members, even in the midst of the unprecedented financial crisis of recent years.

USAA Federal Savings Bank (FSB), an indirect wholly owned subsidiary of USAA, is a federally chartered savings association organized to offer personal retail banking services. FSB was chartered in 1983, and is USAA's only savings association. USAA is, therefore, a grandfathered unitary savings and loan holding company.

The Proposed Rule release (in Footnote 9) indicates that through separate rulemaking or by order, it is expected that the Proposed Rule's requirements would be extended to large savings and loan holding companies and nonbank financial companies supervised by the Board pursuant to Section 113 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Act).[2] As a large savings and loan holding company (SLHC), USAA has significant concerns regarding the implications of any future extension of the Proposed Rule. Specifically, USAA is concerned with the application of Bank Holding Company (BHC) capital requirements to SLHCs and the Board's ability to influence capital distributions, specifically, "dividends" to policyholders and members.

---

[1] Capital Plans, 76 Fed. Reg. 35351 (June 17, 2011).
[2] *Id.* at 35352 n.9.

A. Consider SLHC risk profiles prior to implementation of capital requirements and capital plans.

We appreciate the Board's stated intention in its Supervisory and Regulation (SR) letter 11-11[3] (SR 11-11) to take into account any unique characteristics of SLHCs and coordinate with the primary supervisors and functional regulators of the parent or its nondepository subsidiaries. As expressed in our comment letter submitted on May 23, 2011,[4] USAA has significant concerns that imposing existing BHC capital requirements on insurer SLHCs without rationalizing those guidelines with insurer capital requirements and existing state regulations will result in inappropriate capital requirements and ratings for insurer SLHCs. The assessment of the condition, performance and activities of insurer SLHCs through a consolidated asset-based framework would not capture the unique risk profile of insurers. Because insurers with affiliated depository institutions have traditionally operated in SLHC structures, it is critical the Board incorporate the distinctive features, controls and existing supervision of insurance company operations by modifying BHC supervisory capital requirements for insurer SLHCs.

The business and risk profile of SLHCs often is fundamentally different from that of BHCs. For example, commercial banks typically extend loans to business as well as consumers, which can result in risk concentrations within entities and particular industries. On the other hand, USAA's savings and loan subsidiary, like those of many other SLHCs, lend to consumers, thus mitigating concentration risk. Further, in contrast to most BHCs and SLHCs, Unitary SLHCs operate diversified businesses outside the banking industry as permitted by the Home Owners' Loan Act. For USAA, our insurance enterprises represent a significant portion of our consolidated revenue. The same would not be true for BHCs, which operate primarily in the banking industry. We reiterate the importance of considering these unique aspects of SLHC business and risk profiles when implementing any new supervisory requirements on SLHCs.

We also appreciate the Board in SR 11-11 acknowledges that it will take time for supervisory staff to better understand SLHC's operations and business model.[5] We reiterate our recommendation from our May 23 comment letter that the Board partner with SLHCs and study their unique characteristics to systematically rationalize the BHC capital requirements with insurer SLHC risk profiles prior to the implementation of SHLC capital plans and capital requirements.[6]

---

[3] Board of Governors of the Federal Reserve System, Division of Banking Supervision and Regulation, Division of Consumer and Community Affairs, SR 11-11 / CA 11-5, *Supervision of Savings and Loan Holding Companies (SLHCs)*, dated July 21, 2011.

[4] Letter from Steven Alan Bennett, General Counsel, USAA, to Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, at 1(May 23, 2011), *available at* http://www.federalreserve.gov/SECRS/2011/May/20110526/OP-1416/OP-1416_052311_73334_478586071148_1.pdf.

[5] SR 11-11, *supra* note 3.

[6] Letter from Steven Alan Bennett to Jennifer J. Johnson, *supra* note 4, at 2.

B. Exempt dividends to members and policyholders from the definition of capital distributions.

If the Proposed Rule is extended to large SLHCs, USAA, as an insurer, has concerns about the broad definition of capital distributions. The definition of capital distributions in the Proposed Rule includes "any similar transaction that the Federal Reserve determines to be in substance a distribution of capital."[7]

Like many insurance companies, USAA pays "dividends" and other similar distributions to its policyholders and members. As a state-regulated insurer, USAA's payment of these distributions is subject to regulation under state laws and primarily by the Texas Department of Insurance. USAA's decision to pay dividends and other similar distributions is influenced by a number of factors including the association's financial performance, claims and catastrophe costs, the investment market and the ongoing financial strength of the association.

We are concerned that such policyholder distributions could fall within the broad language of the proposed definition of capital distributions because they are approved annually by the board of directors and funded from annual earnings and policyholder surplus. These distributions, however, are unlike stock dividends. First, these distributions are not based on ownership rights, but represent a return of insurable premiums paid by policyholders, and for that reason are generally tax free to the policyholder. Second, because policyholder distributions effectively decrease the cost of insurance to the consumer, these dividends impact consumer pricing and insurer competitiveness.

Insurance is a highly competitive industry and insurers compete on price. Policyholder dividends help insurance companies keep the effective cost of insurance low for customers. Insurers base premium costs on estimated expenses, including claims and catastrophe costs. If, for example, an insurer has a year with less than expected catastrophe costs that result in excess premiums, rather than keep this excess earned surplus, policyholder distributions allow the insurer to pay the excess back to its policyholders. Therefore, any inability of an insurer SLHC to pay such distributions effectively increases the cost of insurance for consumers.

Further, policyholder distributions help maintain strong customer relations. We believe a return of premium through dividends and distributions builds goodwill and encourages our members to renew their coverage. Maintaining insurance customers not only benefits and strengthens the SLHC, but decreases costs for consumers. Keeping an existing policyholder is less costly than adding a new customer.

Finally, imposing regulations on insurer SLHC distributions, which would not apply to non-SLHC insurers, puts insurer SLHCs at a competitive disadvantage. Strong insurance operations have a positive impact on an insurer SLHC and the depository institution it supports. We therefore urge the Board to expressly exempt dividends and other distributions to members and policyholders from the broad definition of capital distributions.

---

[7] Capital Plans, 76 Fed. Reg. at 35359 (defining capital distribution in Regulation Y Section 225.8(c)(2)).

C. Measure materiality by relating a proposed capital distribution to capital adequacy and the SLHC's ongoing financial strength.

The Proposed Rule, if extended to large SLHCs, requires a SLHC to provide prior notice to the Federal Reserve before making capital distributions if the dollar amount of the capital distribution exceeds the amount described in the capital plan approved by the Federal Reserve. The Board provided an example of a *de minimis* exception relating to a 10 basis point reduction of Tier 1 risk-based capital. An unintended consequence of the proposed *de minimis* exception is that SLHCs with capital far in excess of requirements are unfairly impacted when compared to SLHCs with less excess Tier 1 risk-based capital. While USAA understands the Board's intent, a better measure for materiality would relate the proposed capital distribution to capital adequacy and the SLHC's ongoing financial strength. The *de minimis* exception should be the subject of a sliding scale that increases depending on the SLHC's capital level.

D. Maintain confidentiality of capital plans and stress tests.

Any final rule issued by the Board should expressly provide that capital plans, including stress tests submitted to the Board, will be confidential and not subject to public disclosure. Should capital plans and stress tests be made public, an insurer SLHC would be at a material disadvantage to other non-SLHC insurers. Disclosure of the results of stress test scenarios could give rise to member or policyholder responses that are unwarranted. Moreover, concerns with the consequences of potential public disclosure could influence the Board in its determinations of stress scenario parameters.

E. Delay implementation of capital requirements on SLHCs.

In the Supplementary Information section of the Proposed Rule, the Board acknowledges that the Proposed Rule is not mandated by the Dodd-Frank Act,[8] but relates to the Act insofar as the Act imposes enhanced prudential standards, including stress testing requirements, on large BHCs. As the Board has contemplated imposing the Proposed Rule's requirements on large SLHCs[9] that have not previously been regulated by the Board, we respectfully request that the Board not impose the Proposed Rule on SLHCs, if at all, until five years after the date of the Act's enactment. Such a delay would allow for the alignment the capital plan requirements with the institution of risk based capital requirements, with delayed effectiveness pursuant to Section 171 of the Act.[10] In the Proposed Rule, the Board has applied Section 171 for BHC subsidiaries of foreign banking organizations, thereby providing precedent for using Section 171 to delay application of the Proposed Rule to large SLHCs.

---

[8] *Id.* at 35352.
[9] *Id.*
[10] Section 171 of the Dodd-Frank Act governs risk-based capital (RBC) requirements and provides that the Board establish minimum leverage and RBC requirements on a consolidated basis for SLHCs. The Dodd-Frank Act provides that for any depository institution holding company that was not previously supervised by the Board, the RBC requirements are effective five years after the date of enactment of the Dodd-Frank Act. *See* Section 171(b)(4)(D) of the Dodd-Frank Act. We note that Congress drafted this section with the words "shall be effective" five years after the date of enactment and did not provide for a phase-in period over the course of the five-year period.

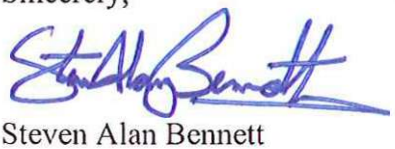
F. Allow SLHCs an opportunity to comment on future proposed rulemakings.

If the Board extends the requirements of the Proposed Rule to large SLHCs as suggested in the Proposed Rule Supplementary Information, we respectfully request the Board issue a formal Proposed Rule and allow SLHCs and impacted entities to comment on the specific implications of such a rule.

* * * * *

USAA appreciates the important role the Board will play in providing for the safe and sound operation of the banking system in the United States. We appreciate the Board's consideration of our comments and look forward to working with the Board in the future. Should you have any questions or wish further clarification or discussion of our points, please contact Michael Broker at 210-498-0029.

Sincerely,



Steven Alan Bennett
Executive Vice President
General Counsel & Corporate Secretary