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VIA ELECTRONIC TRANSMISSION
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October 17, 2012

The Honorable Ben S. Bernanke
Chairman
Board of Governors of the Federal Reserve System
20th Street & Constitution Ave., NW.
Washington, DC 20551

The Honorable Thomas J. Curry
Comptroller
Department of the Treasury
Office of the Comptroller of the Currency
250 E. Street, SW
Washington, D.C. 20219

The Honorable Martin J. Gruenberg
Acting Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW

Re: Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action (Docket No. 1438 & RIN 7100-AD-86); Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements (Docket No. 1438 & RIN 7100-AD-86); Advanced Approaches Risk-based Capital Rule; Market Risk Capital Rule (Docket No. 1438 & RIN 7100-AD-86)

Dear Sirs:

On behalf of Nationwide Mutual Insurance Company ("Nationwide Mutual") and its affiliated companies, we appreciate the opportunity to provide comments to the Office of the Comptroller of the Currency ("OCC"), the Federal Deposit Insurance Corporation ("FDIC"), and the Board of Governors of the Federal Reserve System (the "Board") (collectively, the "Agencies") on the following three notices of proposed rulemaking: (1) Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action (the "Basel III NPR");[1] (2) Regulatory

[1] 77 Fed. Reg. 52792 (Aug. 30, 2012).

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Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements (the "Standardized Approach NPR");[2] and (3) Advanced Approaches Risk-based Capital Rule; Market Risk Capital Rule (the "Advanced Approaches NPR") (collectively, the "Proposed Rules").[3]

Background of Nationwide

As its name suggests, Nationwide Mutual is a mutual insurance company, which was organized under the laws of the State of Ohio in 1925. Nationwide Mutual is the lead entity and ultimate controlling person of all entities in the Nationwide group of companies (collectively, "Nationwide"). Nationwide is a diversified financial services organization offering a wide range of insurance, annuities, and investment products and services.

Nationwide Mutual and its property and casualty insurance subsidiaries primarily underwrite personal automobile, homeowners and commercial insurance products. Nationwide Financial Services, Inc. ("Nationwide Financial"), a subsidiary of Nationwide Mutual, develops and sells a diverse range of products, including individual annuities, private and public sector retirement plans and other investment products sold to institutions, life insurance and advisory services. In addition, Nationwide Financial provides mutual funds through Nationwide Funds Group and banking products and services through Nationwide Bank, a federal savings bank and member FDIC.

By virtue of its ownership of Nationwide Bank, Nationwide Mutual is registered as a savings and loan holding company ("SLHC") pursuant to Section 10 of the *Home Owners' Loan Act of 1933* ("HOLA"), and is the top-tier SLHC of Nationwide Bank for purposes of the Proposed Rules. As of December 31, 2011, Nationwide had approximately $155 billion in total consolidated assets, while Nationwide Bank had approximately $4.5 billion in assets.

We respectfully request that the Agencies consider our comments bearing in mind the following facts: First, Nationwide Mutual, an operating mutual insurance company and lead entity of the Nationwide enterprise, is the top-tier SLHC of Nationwide Bank. Second, Nationwide Bank represents less than 3% percent of the total assets of Nationwide.

Executive Summary

Nationwide has two overarching concerns with the Proposed Rules and a number of subsidiary and more specific concerns. First, the Agencies have failed in the Proposed Rules to adequately and appropriately consider the unique characteristics of SLHCs that are predominantly insurance companies (hereafter, "insurance-centric SLHCs"). Instead, the Proposed Rules inappropriately apply an undifferentiated, bank-centric capital framework to all banking organizations regardless of their predominant line of business. Second, the Proposed Rules fail to account for the fact that insurance-centric SLHCs have never previously been

[2] 77 Fed. Reg. 52888 (Aug. 30, 2012).

[3] 77 Fed. Reg. 52978 (Aug. 30, 2012).

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subject to consolidated, bank-centric capital requirements, and effectively fail to provide any transition period for insurance-centric SLHCs to develop the management information systems ("MIS") necessary to collect information and demonstrate compliance with the Proposed Rules. Indeed, the Proposed Rules ignore the statutory mandate that consolidated capital requirements not be imposed on SLHCs until July 21, 2015.[4] Because of the absence of a transition period, we believe SLHCs will be subject to significantly more stringent treatment under the Proposed Rules than will other banking organizations even though the Dodd-Frank Act explicitly intended that the consolidated capital framework not begin to apply to SLHCs until the middle of 2015.

If adopted as currently proposed, Nationwide strongly believes that the impact of the market distortions created by applying a bank-centric capital framework to insurance-centric SLHCs, coupled with the difficulty of compliance by January 2013, could threaten the existence of the SLHC industry. In addition, we are concerned that the application of an undifferentiated, bank-centric capital framework to all organizations with a depository institution, without regard to their predominant line of business or their unique set of risks, raises safety and soundness concerns for SLHCs, makes it increasingly difficult for SLHCs to serve as a source of financial strength to their depository institution subsidiaries as required by HOLA, and increases the threat of systemic risk in the U.S. financial system.[5]

Nationwide's comments below are divided into two sections. In Section I, Part A we highlight how Congress, through the passage of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the "Dodd-Frank Act"), intended to preserve the charter for savings associations as a source of personal and household credit. To that end, we discuss the necessity for the Agencies to recognize the unique characteristics of SLHCs and provide meaningful transition periods before imposing any consolidated capital framework on them. We point out how the imposition of a bank-centric capital framework on insurance-centric SLHCs is inappropriate due to the fundamental differences between banks and insurers, and how it could have the unintended consequences of driving up prices and limiting product availability for insureds who are seeking protection and planning to live in retirement. We also address the importance of a meaningful transition period for insurance-centric SLHCs. Regardless of whether and how the Agencies tailor the new capital framework for insurance-centric SLHCs, these entities will undoubtedly need more time to come into compliance than they are given under the Proposed Rules. As discussed more fully in this section of our letter, Section 171 of the Dodd-Frank Act (the "Collins Amendment") directs that consolidated capital requirements shall not apply to SLHCs until July 21, 2015. The Agencies appear to ignore this instruction entirely. We argue that the failure to consider the unique characteristics of insurance-centric SLHCs and the absence of a meaningful transition period is likely to harm insurance companies and their customers, and it is reasonable to believe that some insurers have taken steps to divest their savings associations in light of the Proposed Rules.

In Section I, Part B, we highlight how the Dodd-Frank Act was enacted to promote the financial stability of the US financial system and end the problem of "too big to fail." We argue that the

[4] See Section 171(b)(4)(D) of the Dodd-Frank Act.

[5] 12 U.S.C. § 1467a(b)(4)(A)(i)(II)(aa).

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imposition of an undifferentiated, bank-centric capital framework on insurance-centric SLHCs is contrary to these purposes because it could drive asset concentration in the financial system as insurance-centric SLHCs navigate toward the same asset classes as banks. We also demonstrate how the bank-centric capital framework will impede insurance-centric SLHCs' ability to serve as a source of credit for the U.S. economy, and hinder their ability to effectively match long-term liabilities with long-term assets, a fundamental risk management concept in the business of insurance. These unintended consequences could result in an increased threat of systemic risk for the U.S. financial system and destabilize insurance-centric SLHCs, making it difficult for them to ensure their own safety and soundness and serve as a source of financial strength to their depository institution subsidiaries.

For these reasons, and as discussed more fully below, we conclude Section I by urging the Agencies to work more closely with the insurance industry to develop a consolidated capital framework that accurately captures the risks and capital adequacy needs of an insurance company, and that does not contribute to an increased threat of systemic risk for the U.S. financial system.

In Section II of our letter, we reiterate our strong disagreement with the use of an undifferentiated, bank-centric capital framework, but recognize that the Agencies may decide to move forward with such a framework despite our serious reservations. Therefore, we address more specific concerns with the Proposed Rules as applied to insurance-centric SLHCs and, again, urge the Agencies to work more closely with the insurance industry to establish a consolidated capital framework that accurately captures the risk and capital adequacy needs of an insurance company, and that does not contribute to an increased threat of systemic risk for the U.S. financial system.

I. Nationwide's overarching concerns with the Proposed Rules

A. The Proposed Rules' failure to consider the unique characteristics of insurance-centric SLHCs and provide meaningful transition periods could threaten the existence of the SLHC industry

Through enactment of Sections 312 and 313 of the Dodd-Frank Act, Congress abolished the Office of Thrift Supervision ("OTS") and transferred its authority over savings associations to the OCC and its authority over SLHCs to the Board. However, rather than have SLHCs regulated under the same framework as bank holding companies ("BHCs"), Congress preserved the exemption in Section 2(c)(2)(B) of the *Bank Holding Company Act of 1956*, which removes insured savings associations from the definition of a "bank", and maintained the regulatory framework of HOLA for savings associations and SLHCs. These actions of Congress reflect its intention to preserve the charter for savings associations, and its direction to the Agencies that they should take into consideration those unique characteristics of savings associations and SLHCs when regulating them.

In prior comment letters, Nationwide has applauded the Board's early indications that it would take into account the unique situation of SLHCs when acting as their regulator. In its Notice of Intent of April 2011, the Board indicated that it was "considering applying to SLHCs the

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same consolidated risk-based and leverage capital requirements as BHCs *to the extent reasonable and feasible taking into account the unique characteristics of SLHCs and the requirements of HOLA*." [6] In addition, the Board specifically asked for comments regarding whether the "proposed Basel-III based transition periods were appropriate for SLHCs and if not, what alternative transition provisions would be appropriate and why?"[7] Moreover, the Board acknowledged that "[SLHCs] have traditionally been permitted to engage in a broad range of nonbanking activities that were not contemplated when the general risk-based capital requirements for [BHCs] were developed."[8] The foregoing statements seemed to indicate that the Board was developing a consolidated capital framework that would carefully consider the unique characteristics and risks of SLHCs and accommodate their diverse range of business activities.

Again, in its Supervision and Regulation Letter (SR) 11-11, *Supervision of Savings and Loan Holding Companies*, the Board indicated that it intends "to the greatest extent possible, taking into account any unique characteristics of SLHCs and the requirements of HOLA, to assess the condition, performance and activities of SLHCs on a consolidated basis."[9] Similarly, in its December 29, 2011 Information Collection, the Board recognized that it would be unduly burdensome to require SLHCs that are insurance companies with small deposit-taking operations to prepare quarterly consolidated financial statements in accordance with generally accepted accounting principles (GAAP) beginning in 2012 when such companies are not required by law to prepare GAAP financial statements and some only prepare financial statements in accordance with statutory accounting principles (SAP).[10] In this Information Collection, the Board clarified that these "Insurance-SLHCs" would not be required to prepare such reports until the consolidated capital rules were finalized for SLHCs and they were required to demonstrate their compliance with the capital rules.[11]

The above statements and actions of the Board appeared to signal that it would thoughtfully consider the unique characteristics of SLHCs, recognize the fact that SLHCs have never previously been subject to a consolidated capital framework, and provide meaningful transition periods for SLHCs before imposing any such consolidated capital framework on them. However, Nationwide is deeply concerned that the Proposed Rules do not live up to these promises. Instead, the Proposed Rules fail to adequately and appropriately consider the unique characteristics of insurance-centric SLHCs in that they inappropriately impose a capital

[6] Notice of Intent to Apply Certain Supervisory Guidance to Savings and Loan Holding Companies, 76 Fed. Reg. 22,662 (Apr. 22, 2011) (emphasis added).

[7] Id.

[8] Id.

[9] Supervision and Regulation Letter (SR) 11-11, *Supervision of Savings and Loan Holding Companies*, July 21, 2011. http://www.federalreserve.gov/bankinforeg/srletters/sr1111.pdf (emphasis added).

[10] Agency Information Collection Activities Regarding Savings and Loan Holding Companies: Announcement of Board Approval Under Delegated Authority and Submission to OMB, 76 Fed. Reg. 81933, December 29, 2011.

[11] Id. at 81936.

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framework on insurance companies designed specifically for banks; fail to recognize that insurance-centric SLHCs have never previously been subject to such a bank-centric, consolidated capital framework; and treat SLHCs more strictly than other banking organizations by failing to provide any transition period for SLHCs to develop the systems and controls necessary to collect information and demonstrate compliance with the Proposed Rules.

i. The Proposed Rules impose an undifferentiated, bank-centric capital framework that will create market distortions

As will be more fully explained in the context of the Proposed Rules in Section II, a bank-centric capital framework imposed upon insurance-centric SLHCs could negatively impact an insurance company's pricing, product availability, and competitive position relative to other insurers that do not own small depository institutions. First, there are various aspects of the Proposed Rules (*e.g.*, the deduction of insurance underwriting subsidiaries regulatory capital, risk-weighting of separate account assets and policy loans, treatment of available-for-sale securities) that could require insurance companies to hold excess capital in order to account for this inappropriate treatment and absorb increased volatility in their capital ratios. Holding excess capital could lead to higher prices for long-term protection products, or the inability to deploy capital to higher-valued uses.

In addition, there are various aspects of the Proposed Rules that may cause some insurance-centric SLHCs to shift their investment portfolios away from longer-term assets with higher yields (*e.g.*, corporate or municipal bonds) –used to match long-term liabilities – to a portfolio more largely comprised of shorter-term assets with lower yields; similar to that of a bank. Again, lower yields on investments could ultimately lead to higher prices for policyholders who are seeking protection of their valuables and retirement income. In addition, the foregoing could result in asset-liability mismatches as short-term assets cannot be adequately matched against long-term liabilities, which is counter to prudent risk management in the insurance industry. Therefore, an insurance-centric SLHC could be forced to limit product offerings that are long-term in nature, particularly products that offer long-term fixed returns such as fixed annuities, an important retirement planning tool.

To avoid these market distortions, it is imperative that the Agencies establish consolidated capital requirements that accurately reflect the unique characteristics of the business of insurance. We believe it is reasonable to assume that some insurers have taken steps to divest their savings association subsidiaries in light of the Proposed Rules and that the proposals could drive others to do so in order to stay competitive with insurers that do not own relatively incidental savings associations.

ii. The Proposed Rules do not comply with the effective date for SLHCs set forth in the Collins Amendment and also fail to provide any transition period for SLHCs

Another significant concern is that the Proposed Rules would require all SLHCs, including those that are predominantly insurance companies, to comply with this completely new bank-centric, consolidated capital framework as early as calendar year 2013.

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First, Nationwide believes that this ignores Congress' express provision that consolidated capital requirements for SLHCs would not be required until July 21, 2015.[12] Second, even in the absence of such clear Congressional directive, it is imperative that the imposition of an entirely new consolidated capital framework on insurance-centric SLHCs allow for appropriate transition periods so that insurance companies can develop the appropriate MIS infrastructure to collect information and demonstrate compliance without unreasonable expense and resource burdens and ensure the integrity of this data.

Under the Proposed Rules, all banking organizations, including insurance-centric SLHCs would be required to demonstrate compliance with the following risk-based capital and leverage ratios as early as first quarter 2013:

(1) a common equity tier 1 capital ratio of 3.5%;
(2) a tier 1 capital ratio of 4.5%;
(3) a total capital ratio of 8%; and
(4) a tier 1 leverage ratio of 4%.[13]

Nationwide believes that the Proposed Rules fail to provide any meaningful transition period for SLHCs to demonstrate compliance with the minimum regulatory capital ratios. Despite never having been subject to the Basel capital framework, the Proposed Rules would subject insurance-centric SLHCs to the same transition periods as banking organizations that have been operating under the Basel framework for over two decades. Evidently, the Agencies have chosen to ignore Section 171(b)(4)(D) of the Collins Amendment in which Congress, recognizing the practical need for an orderly transition, clearly intends that depository institution holding companies not previously subject to Board supervision be given until July 21, 2015 before being subject to the consolidated capital rules established for these institutions.

While the Agencies have recognized the statutory effective date of July 21, 2015 for bank holding company subsidiaries of foreign banking organizations that are currently relying on the Board's Supervision and Regulation Letter (SR) 01-1 ("SR 01-1 Companies"), Nationwide is very disappointed that they have arbitrarily chosen not to extend the identical statutory effective date to SLHCs.[14] In the Preamble to the Basel III NPR, the Agencies provide that "*[c]onsistent with the Dodd-Frank Act*, a bank holding company subsidiary of a foreign banking organization that is currently relying on the Board's Supervision and Regulation Letter SR 01-1 would not be required to comply with the proposed capital requirements under any of these NPRs until July 21, 2015."[15] In so stating, the Agencies reference Section 171(b)(4)(E) of the Dodd-Frank Act, which provides as follows:

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[12] See Section 171(b)(4)(D) of the Dodd-Frank Act.

[13] 12 C.F.R., Part 217.10 and 217.300.

[14] 12 C.F.R., Part 217.300.

[15] 77 Fed. Reg. 52795 (August 30, 2012) (emphasis added).

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> (E) CERTAIN BANK HOLDING COMPANY SUBSIDIARIES OF FOREIGN BANKING ORGANIZATIONS. – For bank holding company subsidiaries of foreign banking organizations that have relied on Supervision and Regulation Letter SR-01-1 issued by the Board of Governors (as in effect on May 19, 2010), the requirements of this section, except as set forth in subparagraph (A), shall be effective 5 years after the date of enactment of this Act.

Section 171(b)(4)(D) provides nearly identical language for depository institution holding companies,[16] which by definition includes SLHCs, that were not supervised by the Board prior to May 19, 2010 and, as a result, were not previously subject to consolidated capital requirements under the Basel framework. Section 171(b)(4)(D) reads as follows:

> (D) DEPOSITORY INSTITUTION HOLDING COMPANIES NOT PREVIOUSLY SUPERVISED BY THE BOARD OF GOVERNORS – For any depository institution holding company that was not supervised by the Board of Governors as of May 19, 2010, the requirements of this section, except as set forth in subparagraphs (A) and (B), shall be effective 5 years after the date of enactment of this Act.

In the Proposed Rules, the Agencies have decided to honor the intent of Congress in Section 171(b)(4)(E) and not require SR 01-1 Companies to comply with the Proposed Rules until July 21, 2015. Inexplicably, however, the Agencies have decided to ignore the same Congressional intent, represented by nearly identical language in Section 171(b)(4)(D), as it applies to SLHCs that were not previously subject to Board supervision, and require compliance less than three months from the date of this letter, beginning calendar year 2013. Although the Agencies do not explicitly point to the Board's general authority under Section 10(g)(1) of HOLA (as amended by Section 616(b) of the Dodd-Frank Act) to establish countercyclical capital standards for SLHCs, it is possible that in ignoring Section 171(b)(4)(D) of the Collins Amendment, the Board is attempting to rely on that general authority. However, because the Proposed Rules do not appear to be countercyclical in nature, we do not believe they are an appropriate exercise of that authority in any event.

In construing the specific five-year time frame set forth in Section 171(b)(4)(D) and the general authority set forth in Section 616(b), there are several canons of statutory construction that support the conclusion that a July 21, 2015 effective date is not only required but also is the most appropriate for SLHCs. First, it is a maxim of statutory construction that specific terms in a statute override general terms ("Where there is no clear intention otherwise, a specific statute will not be controlled or nullified by a general one, regardless of the priority of enactment." *Morton v. Mancari*, 417 U.S. 535, 550-551 (1974) (per J. Blackmun)). Thus, a provision granting general authorization cannot be read to trump a provision containing an explicit requirement. Second, a statute should be read as a whole, and not selectively ("In ascertaining the plain meaning of the statute, the court must look to the particular statutory language at issue, as well as the language and design of the statute as a whole." *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 291 (1988) (J. Kennedy)). Finally, it is axiomatic that every word in a statute is to be given effect ("These words cannot be

[16] 12 U.S.C. § 5371(a)(3) defines depository institution holding companies as "a bank holding company or savings and loan holding company (as those terms are defined in Section 3 of the Federal Deposit Insurance Act) that is organized in the United States, including any bank or savings and loan holding company that is owned or controlled by a foreign organization, but does not include the foreign organization."

meaningless, else they would not have been used." *United States v. Barber*, 297 U.S. 1, 65 (1936) (J.Roberts)).

Thus, even if we assume that the Board is relying on its general HOLA authority, the specific time frame for the imposition of consolidated capital requirements on SLHCs in Section 171(b)(4)(D) should override the general requirement in Section 10(g)(1) of HOLA, as amended. While we recognize that these two provisions are contained in different statutes, both provisions were amendments included as part of the same and singular Dodd-Frank Act and were enacted at the same time by Congress. It would make no sense for Congress to establish a specific five-year effective date that could be disregarded by the Agencies in reliance on a more general provision that does not explicitly allow the effective date to be overridden, especially when the general provision was adopted at the same time in the same statutory scheme. Such a result would render the express five-year provision meaningless. Therefore, consistent with Section 171(b)(4)(D) of the Dodd-Frank Act, we urge the Agencies to revise the Proposed Rules to provide a July 21, 2015 effective date for SLHCs instead of requiring SLHCs to comply with the Proposed Rules as early as January 2013.

Additionally, we believe an effective date beginning calendar year 2013 is particularly unreasonable and impracticable for insurance-centric SLHCs that are mutual insurance companies. Many mutual insurance companies are not required by law to prepare financial statements in accordance with GAAP and only produce financial statements in accordance with SAP (or prepare financial statements in accordance with GAAP on a limited basis). These companies will unlikely be in a position to comply with the filing requirements associated with the Proposed Rules in the short time frame provided by the Agencies. Moreover, in the event a mutual insurance company would need to improve its common equity tier 1 risk-based capital ratio, it could only do so through the retention of earnings or changes to its asset exposures as mutual insurance companies by definition do not have access to the capital markets. Due to the short time frame for compliance, changes to asset exposures are likely the only viable option. This could result in an insurance company divesting assets or rebalancing its investment portfolio in an unsafe and unsound manner. Therefore, we believe it is necessary to provide insurance-centric SLHCs, especially those that are mutual insurance companies, a meaningful transition period so that they can ensure compliance in manner that is efficient and prudent from a risk management standpoint, and that is not unduly burdensome and costly from a resources standpoint. That effective date should be no earlier than July 21, 2015, consistent with the Collins Amendment.

Further, the need for a meaningful transition period for SLHCs that have never been subject to Board supervision applies with equal, if not greater, force than it does to SR 01-1 Companies. The Proposed Rules would for the first time impose capital requirements designed specifically for banking institutions on SLHCs that are predominantly engaged in the business of insurance. As we have outlined, the Basel frameworks were not designed for a consolidated organization like Nationwide where the top-tier SLHC is an operating mutual insurance company that owns a depository institution representing less than three percent (3%) of the total consolidated assets of an enterprise predominantly engaged in the business of insurance. Because Nationwide, like most insurance-centric SLHCs, is only nominally engaged in traditional banking activities relative to its total assets, it is not surprising that it would need

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sufficient time to design new, or redesign its current, financial reporting and MIS in order to calculate and report the minimum capital requirements under the Proposed Rules.

In order to demonstrate compliance with the Proposed Rules and report its results to the Board, it appears that Nationwide would be required to file the FR Y-9C as early as first quarter 2013. As an "Insurance SLHC,"[17] Nationwide is currently exempt from preparing the FR Y-9 series of reports. In its Information Collection of December 29, 2011, the Board indicated that "Insurance SLHCs will be exempt only until consolidated regulatory capital requirements are finalized for SLHCs, *at which time they may be required to file consolidated financial statements to demonstrate their compliance with the capital rules* ...."[18] It is reasonable for Insurance SLHCs to have believed that they would not need to demonstrate compliance with the Proposed Rules until July 21, 2015, based on the clear language in Section 171(b)(4)(D) set forth above, and therefore would not have to prepare and file the FR Y-9 series of reports until that time. Nevertheless, the Proposed Rules appear to contemplate that all SLHCs, including those defined as Insurance SLHCs under the Board's Information Collection, will need to begin demonstrating compliance with the Proposed Rules through the filing of the FR Y-9C in the first quarter of 2013, which must be prepared in accordance with GAAP. As stated above, we do not believe that Insurance SLHCs will be in a position to comply with these filing requirements in a matter of mere months as contemplated by the Proposed Rules. As we have highlighted, many insurance companies are not required by law to prepare financial statements in accordance with GAAP, and some only produce financial statements in accordance with SAP.

If adopted as proposed, SLHCs will likely be required to fully implement the Proposed Rules under a more aggressive time frame than all other banking organizations. The applicability provision of the Standardized Approach NPR provides as follows:

> (b) On January 1, 2015, and thereafter, a [banking organization] must calculate risk-weighted assets under subpart D of this part. On or before December 31, 2014, the [banking organization] must calculate risk-weighted assets under either:
> (i) The methodology described in the general risk-based capital rules under 12 CFR part 3, appendix A, 12 CFR part 167 (OCC); 12 CFR part 208, appendix A, 12 CFR part 225, appendix A (Board); 12 CFR part 325, appendix A, and 12 CFR part 390 (FDIC); or
> (ii) Subpart D of this part.

For purposes of reporting risk-based capital ratios, the foregoing language would allow all banking organizations to continue using the current-risk based capital framework to calculate risk-weighted assets until January 1, 2015, or alternatively choose to adopt the

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[17] 76 Fed. Reg. at 81936, which provides that "Certain Insurance SLHCs" will not be required to initially transition to the Federal Reserve regulatory reports if: (1) as calculated annually as of June 30th, using the assets reported as of June 30th, where more than 50 percent of the assets of the SLHC are derived from the business of insurance on an enterprise-wide basis; *and* (2) the SLHC does not submit reports to the SEC pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

[18] Id. (emphasis added).

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standardized approach for calculating risk-weighted assets as soon as January 1, 2013. Because SLHCs have never been subject to the current-risk based capital framework, they will be in the unworkable position of having to configure and adopt within two months, one of two entirely new approaches to compute their risk-weighted assets. If they opted to use the current rules until January 1, 2015 (an alternative permitted to and more practicable for banks and bank holding companies), then they would have to completely configure their MIS to be able to do so in a matter of months only to immediately reconfigure their MIS to begin using the standardized approach in 2015. Because this would likely be prohibitively expensive and impractical for SLHCs, they would effectively be forced to early adopt the standardized approach with no phase-in time at all. The practical import of this provision highlights the absurdity of permitting banking organizations already in compliance with bank-capital rules to transition to a new method of calculating their risk-weighted assets until January 1, 2015, but not allowing similar treatment for SLHCs not previously subject to the any bank-centric capital regime. This presents yet another reason why SLHCs should be given the full benefit of July 21, 2015 effective date as directed by Congress.

As discussed above, we believe that a five-year transition period is called for not only because it is mandated by the Collins Amendment, but also because SLHCs have never previously been subject to bank-centric, consolidated capital requirements and are typically only incidentally engaged in traditional banking activities. Thus, they will need time to understand the intricacies and nuances of these bank-centric Proposed Rules as they apply to an insurance business model. Moreover, SLHCs do not have in place the MIS specifically designed to report and demonstrate compliance with the Proposed Rules and it would be unduly burdensome, if not impossible, for them to develop a workable system in two months. For these reasons, Nationwide respectfully requests that the Agencies revise the Proposed Rules to provide for a July 21, 2015 effective date for depository institution holding companies not subject to Board supervision on May 19, 2010.

b. The Proposed Rules' imposition of an undifferentiated, bank-centric capital framework will increase the threat of systemic risk in the U.S. financial system

Nationwide strongly believes that the Agencies' decision to impose an undifferentiated, bank-centric capital framework on all depository institution holding companies, regardless of their predominant line of business, could have the unintended consequence of increasing systemic risk in the financial system and thereby perpetuate the exact problem that the passage of the Dodd-Frank Act was intended to address. In the Preamble to the Standardized Approach NPR, the Board describes how it rejected suggestions by commentators to defer to the capital standards of insurance regulators because such an approach would "be inconsistent with the requirements set out in section 171 of the Dodd-Frank Act." Despite those recommendations, the Agencies concluded that "it is important to apply consolidated risk-based and leverage capital requirements to insurance-based holding companies," and "a uniform approach for all holding companies would mitigate potential competitive equity issues, limit opportunities for regulatory arbitrage, and facilitate comparable

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treatment of similar risks."[19] While the Agencies may believe they have met the tactical objectives of Section 171 of the Dodd-Frank Act, we believe that the decision to require an undifferentiated, bank-centric standard is misguided and in fact thwarts the Dodd-Frank Act's strategic objectives of preventing systemic risk. The Preamble to the Dodd-Frank Act states that it was enacted "to promote the financial stability of the United States" and end "too big to fail."[20] We strongly argue that a one-size-fits-all approach to consolidated capital requirements is directly counter to the aforementioned goals, and could actually increase the threat of systemic risk.

As Nationwide and others in the industry have commented in prior correspondence at length, the businesses of banking and insurance are fundamentally distinct. The insurance and reinsurance business models have features that make them a source of systemic stability as opposed to a source of systemic risk.[21] Insurers are funded through upfront premium inflow and, unlike banks, do not rely on wholesale funding and demand deposits to finance their operations.[22] Insurers invest received premiums in long-term assets to cover their long-term obligations using an asset-liability matching approach.[23] The nature of insurance claims results in outflows over an extended period of time and insurance products have mechanisms such as surrender charges to protect against illiquidity.[24] As a result, insurance companies are not as susceptible to a "run on the bank" scenario. Moreover, while banks and insurance companies both face risks on the liability sides of the balance sheet, those risks are entirely distinct. The risks facing banks are generally related to liquidity while insurance companies face an entirely different set of liability risks (*e.g.*, catastrophe risk, morbidity risk, mortality risk). For a bank, the asset risk and liability risk that flow from its liquidity risk are highly correlated, and a run on the bank is most likely to occur when the asset quality of the bank is suffering. For an insurance company, the asset risk is uncorrelated with the actuarially derived liability risk.

The differences between banking and insurance laid out above make it clear that an insurance company's financial strength cannot be predicated on its asset risks alone, but must start with an understanding of its liabilities and how it reserves for those liabilities. Therefore, a consolidated capital framework based solely on asset risks may be appropriate for a bank, but it is not appropriate for insurance companies. In a joint report with the NAIC, the Board itself recognized that its banking capital framework and the insurance risk-based capital framework "differ fundamentally in the risks they are designed to assess, as well as their treatments of

[19] Regulator Capital Rules: Standardized Approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements, 77 Fed. Reg. 52928 (Aug. 30, 2012).

[20] H.R. 4173, 111th Congress, (2010).

[21] See, Geneva Association report, *Geneva Association Response to the IAIS G-SII Consultation* (July 2012).

[22] See, Geneva Association report, *Systemic Risk in Insurance: An analysis of insurance and financial stability* (March 2010).

[23] Id.

[24] Id.

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certain risks common to both sectors."[25] The joint report concluded that the "effective regulatory capital requirements" for insurers and banks are not the same and "the effective capital charges cannot be harmonized simply by changing the nominal charges on individual assets."[26]

For the foregoing reasons, Nationwide believes that the use of a "bank-centric" capital framework is manifestly inappropriate for insurance companies. Due to fundamental differences between insurance and banking, the riskiness of an asset will look very different for a bank than it does for an insurance company. Likewise, an asset's risk may look very different for a property and casualty insurer than it does for a life or health insurer. The insurance industry has accounted for this reality through its risk-based capital system that has a specifically designed capital framework for property and casualty insurers, life insurers and health insurers, which recognizes their unique risk profiles.[27] Moreover, the State-based insurance risk-based capital system is not limited to asset risk, but also takes into account liability risks and other insurance-specific business risks. Under the State risk-based capital system, statutory accounting is used to value both assets and liabilities in a conservative manner, which takes a long-term, asset-liability matching posture that appropriately encourages companies to invest for the long-term. On the other hand, the Agencies' bank capital framework does not recognize the concept of asset-liability management, and instead relies on GAAP accounting and fair value adjustments that can create significant volatility in an insurance-centric SLHC's regulatory capital.

We believe that the use of an undifferentiated, bank-centric framework would inappropriately invite and encourage some insurance-centric SLHCs to shift their investment portfolios away from longer-term assets to a larger portfolio of short-term assets, which could result in asset-liability mismatches as short-term assets cannot be adequately matched against long-term liabilities. The foregoing is counter to prudent risk management in the insurance industry and would have the ultimate impact of hindering an insurance company's ability to act as a source of systemic stability during times of financial distress. In addition, the inability to appropriately match long-term liabilities with long-term assets could affect an insurance-centric SLHC's safety and soundness, and thereby affect the safety and soundness of its depository institution subsidiary. Indeed, the Financial Stability Oversight Council (FSOC) has expressly recognized that maturity mismatches increase a financial company's vulnerability to financial distress and, therefore, liquidity risk and maturity mismatches are one of the categories in the analytical framework for determining whether a nonbank financial company should be designated for consolidated supervision by the Board.[28]

As stated above, the business of insurance can actually serve as a source of systemic stability for the economy as opposed to a source of systemic risk. Due to this fact,

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[25] Report of the NAIC and the Federal Reserve System Joint Subgroup on Risk-based Capital and Regulatory Arbitrage (May 24, 2002), at 1.

[26] Id.

[27] See http://www.naic.org/documents/committees_e_capad_RBCoverview.pdf.

[28] Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies, 77 Fed. Reg. 21637 (April 11, 2012).

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there are significant diversification reasons for permitting strong insurance companies to own and operate savings association subsidiaries. As long as insurance companies are regulated under a capital adequacy framework that appropriately considers their unique risk profiles, these insurance companies will be able to serve as a source of strength to their savings association subsidiaries, as required by Section 38A of the *Federal Deposit Insurance Act* (as amended by section 616 of the Dodd-Frank Act) during those times when the banking industry may be facing periods of financial distress. The imposition of an undifferentiated, bank-centric capital framework on insurance-centric SLHCs will impair this diversification benefit to the extent that it drives insurance companies to invest in the same asset classes as banks, and will remove an important source of systemic stability in the economy.

Also, the insurance industry is an important investor in the U.S. economy for long-term corporate debt and equity, municipal bonds, and other long-dated instruments such as commercial mortgage loans. Due to the constraints of a bank-centric capital framework, it could significantly curtail the insurance industry's appetite for these types of instruments, which will raise the cost of capital for U.S. corporations, municipalities and entrepreneurs and, in times of financial distress, can further contribute to increased systemic risk by reducing the capital supplied by insurance companies to help finance the U.S. economy – contrary to express Congressional design.

Finally, an undifferentiated, bank-centric framework will incent all companies subject to such a framework to invest in the same assets, even if these companies would typically invest in assets different from those in which a bank would invest. Thus, there will be less diversification in the financial system, thereby artificially bidding up the values of assets that are attractive under the one-size-fits-all capital framework. This has the potential to create distortions and cause bubbles as all "banking organizations" flock to the same assets, and exacerbate busts during downturns as assets will be concentrated in "banking organizations" that are driven to make similar divestment actions under their common capital framework. It is notable that historically banks found residential mortgage loans and securities attractive given the favorable capital treatment these assets received. This concentration, fostered by a well-intentioned bank-centric capital regime, exacerbated systemic risk when the housing downturn occurred.

Thus, in order to prevent additional sources of systemic risk that would be caused by a one-size-fits-all capital framework, and to ensure the safety and soundness of insurance-centric SLHCs and their depository institution subsidiaries, Nationwide strongly urges the Agencies to propose a consolidated capital framework that appropriately considers the unique risks and characteristics of the business of insurance. We believe that any such framework must take into consideration the State risk-based capital regime for insurance companies, which was specifically designed and tailored over the past 20 years to the risk profile of insurers. We believe that the State-based system achieves and furthers the goals of the Collins Amendment in ensuring well-capitalized institutions under a strong capital standard, but does so in recognition of the true risk picture of a firm predominantly engaged in the business of insurance. Such an approach has the effect of preserving the savings and loan charter, ending "too big too fail" and promoting systemic financial stability, all within the express design of Congress.

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II. Specific issues with the Basel III framework as applied to insurance-centric SLHCs

As outlined in Section I, we believe that the imposition of an undifferentiated, bank-centric capital framework is inappropriate for insurance-centric SLHCs, will lead to market distortions, and may actually increase systemic risk and raise prudential insurance company safety and soundness concerns. In this Section II, we wish to point out specific aspects of the Proposed Rules that are particularly problematic for insurance-centric SLHCs and how they create those concerns outlined in Section I.

A. The Proposed Rules should not require insurance underwriting subsidiaries to deduct their minimum regulatory capital from total capital

The Basel III NPR would require SLHCs and BHCs to consolidate and deduct the minimum regulatory capital requirements of their insurance underwriting subsidiaries (generally 200 percent of the subsidiary's authorized control level risk-based capital as established by the appropriate state insurance regulator) from total capital to reflect the capital needed to cover insurance risks.[29] According to the Board, the rationale for the deduction is that it is consistent with the advanced approaches rule and "it recognizes that capital requirements imposed by the functional regulator to cover the various risks that insurance risk-based capital captures reflect capital needs at the particular subsidiary and that this capital is therefore not generally available to absorb losses in other parts of the organization."[30]

We strongly oppose the required deduction as it will result in a double counting of the asset risk to which insurance-centric SLHCs are exposed, and, therefore, the need to hold capital twice for the same asset risks. The Board, in the preamble to the 2007 final advanced approaches rules provided that it

> does not agree that the proposed approach results in a double-count of capital requirements. Rather, the capital requirements imposed by a functional regulator or other supervisory authority at the subsidiary level reflect the capital needs at the particular subsidiary. The consolidated measure of minimum capital requirements should reflect the consolidated organization.[31]

As an initial matter, we find it concerning that the Board's rationale for the proposed deduction is because it is consistent with its 2007 advanced approaches final rule. The 2007 advanced approaches rule was applicable only to the largest, most-complex banking institutions and, as far as we can tell, none of the institutions required to implement the 2007 advanced approaches rules had substantial insurance underwriting subsidiaries. Therefore, the impact of this deduction would not have been as salient to the 2007 advanced approaches institutions as it is to insurance-centric SLHCs.

[29] 12 C.F.R., Part 217.22(b)(3).

[30] 77 Fed. Reg. 52929 (August 30, 2012).

[31] 72 Fed. Reg. 69325 (December 7, 2007).

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Second, we respectfully disagree with the Board that the proposed capital deduction does not result in a double-count of capital requirements. Under the State risk-based capital framework, asset risks are specifically included in the calculation of an insurance company's minimum required risk-based capital. The State risk-based capital framework for a property and casualty insurer, like Nationwide Mutual, measures six specific categories of risk:[32]

- R0 – Asset Risk – Affiliates
- R1 – Asset Risk – Fixed Income Investments
- R2 – Asset Risk – Equity Investments
- R3 – Asset Risk – Credit
- R4 – Underwriting Risk – Reserves
- R5 – Underwriting Risk – Net Written Premium

Likewise, for a life insurer, like Nationwide Life Insurance Company, the risk-based capital framework measures five specific categories of risk:[33]

- C0 – Asset Risk – Affiliates
- C1 – Asset Risk – Other
- C2 – Insurance risk
- C3 – Interest Rate Risk; Health Credit Risk; and Market Risk
- C4 – Business Risk

Under the above risk-based capital frameworks, asset-specific risks are accounted for in the R0, R1, R2, and R3 categories for property and casualty insurers, and in C0, C1, and C3 categories for life insurance companies. Therefore, the insurance company capital that covers this asset risk under the State risk-based capital framework would have to be deducted from the calculation of total capital under the Proposed Rules, while these same assets would be consolidated at the top-tier entity and included in the minimum regulatory capital ratios. As shown in **Appendix A**, the proposed deduction of the insurance company's regulatory capital would inequitably require an insurance company to hold more capital for the same amount of asset risk as a BHC or SLHC without an insurance underwriting subsidiary.

[32] See Note 27, supra.

[33] See Note 27, supra.

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Requiring insurance-centric SLHCs to deduct the regulatory capital held by their insurance underwriting subsidiaries would also create significant market distortions. The insurance underwriting subsidiaries for these SLHCs constitute a significant portion of the capital and assets of the consolidated organization, unlike a large complex banking organization. A requirement that insurance-centric SLHCs maintain redundant levels of capital will result in additional expenses and opportunity costs, which could ultimately lead to higher prices for insurance products, or the inability to deploy capital to more efficient uses that could lower prices for these same customers or increase the availability of insurance products. The foregoing will impact the competitiveness of insurance-centric SLHCs *vis-à-vis* non-SLHC insurance companies. Likewise, it may affect these insurers' ability to offer long-term retirement products like variable annuities to consumers, as the proposed deduction associated with these products would impose severe capital penalties on insurers.

We respectfully request that the Agencies amend the Proposed Rules to remove the deduction of the insurance underwriting subsidiaries regulatory capital. Should the Agencies nevertheless decide to move forward with such a deduction, then, at a minimum, there should be a corresponding deduction to the denominator of the regulatory capital ratios to remove the asset risk that has already been factored in to the risk-based capital ratios under the State risk-based capital framework. In the alternative, the deductions from total capital should only include those risk categories that do not capture asset risk: R4 and R5 for property and casualty insurers and C2 and C4 for life insurers.

B. Unrealized gains and losses on available-for-sale debt securities should not be included in common equity tier 1 capital

Under the Proposed Rules, unrealized gains and losses on all available-for-sale (AFS) securities would flow through to common equity tier 1 capital, including unrealized gains and losses related to debt securities whose valuations change as a result of fluctuations in a benchmark interest rate.[34] The foregoing represents a change from the Agencies' current general-risk based capital rules where unrealized gains and losses on AFS debt securities are not included in regulatory capital, unrealized losses on AFS equity securities are included in tier 1 capital, and unrealized gains on AFS equity securities are partially included in tier 2 capital. The Preamble to the Basel III NPR states that the Agencies believe "this proposed treatment would better reflect an institution's actual risk."[35] However, the Agencies recognize such an approach "could introduce substantial volatility in a banking organization's regulatory capital ratios."[36]

Nationwide agrees that the inclusion of unrealized gains and losses on all AFS securities will introduce increased volatility in a banking organization's regulatory capital ratios, which will be compounded for insurance companies which typically hold significantly larger portfolios of long-term securities than do banks. In a rising interest rate environment, an

34 77 Fed. Reg. 52811 (August 30, 2012).

35 Id.

36 Id.

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insurance company's regulatory capital ratios could fluctuate significantly. The problem will be significant as the economy transitions away from the current environment where interest rates are at historic lows. As laid out in Section I above, an insurance company's liabilities tend to be longer-term in nature with controlled outflows. To offset these long-term liabilities, an insurance company invests in longer-term assets. By appropriately matching assets to liabilities, it significantly prevents unrealized gains and losses due to interest rate movements from ever being realized.

The inclusion of unrealized gains and losses on all AFS securities in common equity tier 1 capital provides a prime example of how an undifferentiated, bank-centric capital framework can create market distortions for insurance companies and result in increased systemic risk. In order to avoid the potential impact of volatile interest rate swings, some insurers may be forced to raise additional capital, exit markets, shift to held-to maturity (HTM) accounting for some or all of their assets, or shift their investment portfolios away from long-term, interest rate sensitive assets to short-term, low-yield investments. The cost of raising additional capital or the lost yield on long-term investments could eventually lead to higher prices for customers or the inability to deploy capital to higher valued uses that could lower prices for these same customers. Likewise, it may cause insurance companies to limit product offerings that are long-term in nature, particularly products that offer long-term fixed returns such as fixed annuities, an important retirement planning tool. Switching to HTM accounting would reduce insurance companies' flexibility in managing their investment portfolios in reaction to changing market conditions. Even more troubling, providing incentives for insurance companies to shift away from longer term assets to shorter-term assets that do not match their long-term liabilities would be counter to the fundamental concept of asset-liability management in managing insurance company risk and could destabilize insurance companies and impact their ability to ensure the safety and soundness of their insured depository institution. As stated above, the FSOC has expressly recognized that maturity mismatches increase a financial company's vulnerability to financial distress.[37]

The foregoing represents yet another reason why the Basel framework is inappropriate for insurance companies. The Basel framework includes no recognition of the fundamental concept of matching longer-term assets to the liability side of the insurer balance sheet, which is one of the most important constructs in the entire insurance risk management framework. Nationwide recommends that any consolidated capital framework imposed on insurance-centric SLHCs exclude unrealized gains and losses related to all debt securities, including debt securities whose valuations primarily change as a result of fluctuations in a benchmark interest rate, including but not limited to Treasuries, securities issued or guaranteed by Fannie Mae and Freddie Mac, obligations of U.S. states and municipalities and investment grade debt securities. Given that insurance companies do not experience runs on liabilities in the same manner as a bank, and that actuarial liability risks are not correlated with the risk of asset quality in an insurance company, it is not necessary and would be harmful to consider the market value of fixed-income securities in capital for insurance companies.

[37] Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies, 77 Fed. Reg. 21637 (April 11, 2012).

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C. The Proposed Rules do not appropriately consider the unique characteristics of separate account assets

The Agencies propose assigning a zero percent risk weight to assets held in "non-guaranteed" separate accounts where all the losses are passed on to the contract holders.[38] The Proposed Rules also provide that the assets in separate accounts that are not considered "non-guaranteed" will be risk-weighted using the current risk-weighting treatment for assets held in a separate account that does not qualify as non-guaranteed – that is, the separate account assets are assigned to risk-weight categories based on the risk-weight of the underlying assets.[39]

To qualify as a separate account under the Proposed Rules, the following conditions must generally be met:

(1) the account must be legally recognized under applicable law;
(2) the assets in the account must be insulated from general liabilities of the insurance company under applicable law and protected from the insurance company's general creditors in the event of the insurer's insolvency;
(3) the insurance company must invest the funds within the account as directed by the contract holder in designated investment objectives or policies; and
(4) all investment performance, net of contract fees and assessments, must be passed through to the contract holder, provided that contracts may specify conditions under which there may be a minimum guarantee, but not a ceiling.[40]

In addition, to qualify as "non-guaranteed" under the Proposed Rules, the following must be true of the separate account:

(1) the insurance company could not contractually guarantee a minimum return or account value to the contract holder, and
(2) the insurance company would not be required to hold reserves for these separate account assets pursuant to its contractual obligations on an associated policy.[41]

While we support a zero percent risk-weighting for non-guaranteed separate accounts, the requirement that the insurance company cannot be required to hold reserves for separate account assets pursuant to its contractual obligation on an associated policy is overly broad. Insurance companies that offer variable life and variable annuity products, funded by separate accounts, offer certain contractual promises that are not guarantees of the value of the assets in the separate account, but are promises to pay an additional benefit in the event of a specific event. State insurance law provides that these obligations must be accounted for in the insurance company's capital and general account reserves, which are backed by general

[38] 77 Fed. Reg. 52929 (Aug. 30, 2012).

[39] Id.

[40] Id.

[41] Id.

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account assets that will be risk-weighted. Therefore, to apply an additional capital charge to the underlying separate account assets, despite the fact that the insurance company is not guaranteeing the value of the separate account assets, does not make sense. The Proposed Rules result in a capital charge on the general account assets backing the general account reserve obligations and a second capital charge on the non-guaranteed separate account assets as well. Requiring insurance-centric SLHCs to hold capital against non-guaranteed separate account assets could lead to higher prices for policyholders as these companies would require a return on this capital that is not required or charged to customers today. Therefore, either an inappropriate definition or risk-weighting of non-guaranteed separate accounts could adversely impact the pricing and availability of minimum guaranteed death benefits in variable life insurance and variable annuity products. We do not believe this is what the Agencies intended.

Likewise, applying a capital charge to separate accounts assets that are in separate accounts that do not meet the criteria for "non-guaranteed separate accounts" does not appropriately reflect their risk. We recognize that such separate accounts present risk to an insurer and it is appropriate for an insurer to hold capital against those risks. However, the risk to the insurer is derived from the value of the guarantee related to those separate accounts assets as opposed to the value of the underlying assets. Thus, any capital charge under any capital framework should be applied to the value of the guarantee, not to the value of the underlying assets. The State risk-based capital framework specifically accounts for the risks posed by these kinds of separate accounts through the C3 (Interest Rate and Market Risk) capital charge. Risk weighting the underlying assets in those separate accounts would have the counter intuitive effect of requiring higher capital when the risk posed by the guarantee is lower. To illustrate, as the value of the assets in those separate accounts increases, the potential risk of the guarantee being realized is reduced as the guarantee is "further out of the money"; however, under the Proposals, the risk weighting would inappropriately be applied to the market value of the assets, which would result in higher capital charges despite the decline in the value and risk of the guarantee. The amount of the potential risk from these guarantees is determined through a defined stochastic analysis, which results in an appropriately applied C3 charge under the state risk-based capital framework. We believe this highlights a further example of how the proposed rules inappropriately reflect the business of insurance.

Further, Nationwide believes that separate account assets, whether or not they qualify as "non-guaranteed", should be excluded from the denominator of the tier 1 leverage ratio. The tier 1 leverage ratio denominator would be comprised of the average consolidated assets as reported on the FR Y-9C, less amounts deducted from tier 1 capital. Thus, the Proposed Rules appear to require insurance-centric SLHCs to include separate account assets in their tier 1 leverage ratio denominator if the separate account assets are reported on the FR Y-9C. These separate account assets are not subject to the claims of the insurance organization's general creditors. Moreover, the company is required to hold a liability equal to the separate account assets fair market value and the sale of the separate account assets would be the source of liquidity for satisfying withdrawals or policyholder benefits for these products, and the insurance company would have no debt or leverage liabilities associated with those assets. The value of the liability associated with the separate account would be satisfied by the value of the separate account assets when liquidated with no other obligation for the

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insurer aside from the guarantees discussed above. Therefore, Nationwide urges the Agencies to exclude these assets from the tier 1 leverage ratio calculation. This proposed exclusion is consistent with the principal objective of the tier 1 leverage ratio, which is to constrain a banking organization's ability to leverage its equity capital base. The ratio is intended to limit risk, and can be used as a supplement to the general risk-based capital ratios. For these reasons, the FSOC specifically excluded separate accounts from the leverage ratio calculation in its recent final rule and interpretive guidance on the designation of non-bank financial companies for Board supervision, stating that such an exclusion was appropriate because separate accounts are "not available to claims by general creditors of a nonbank financial company."[42]

D. The treatment of corporate exposures is unfair for insurers subject to the Proposed Rules

The Proposed Rules would assign a 100 percent risk weight to all corporate exposures, which are defined as exposures to *a company* that is not a sovereign, the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, an MDB, a depository institution, a foreign bank, a credit union, a PSE, a GSE, a residential mortgage exposure, a pre-sold construction loan, a statutory multi-family mortgage, an HVCRE exposure, a cleared transaction, a default fund contribution, a securitization exposure, an equity exposure, or an unsettled transaction.[43]

Nationwide believes that a 100 percent risk weight on investment grade corporate bonds is inappropriate. While we recognize that the 100 percent risk weighting has been a longstanding practice under the Agencies' capital frameworks, it is important to point out that this risk-weighting will have a disproportionately negative impact on insurers as it does banks. Insurance companies invest heavily in corporate bonds due to their need to match long-term liabilities with long-term assets for risk management purposes. Because insurers have substantially larger holdings of investment grade corporate bonds as compared to banks, the inappropriateness a 100 percent risk weighting on investment grade corporate bonds would not have been as salient to the banking industry as it is to the insurance industry. Our initial research indicates that losses from investment grade corporate bonds is materially less than the loss experience of commercial and industrial bank loans, which receive similar treatment under the Proposed Rules. Additionally, insurers are an important source of credit for U.S. corporations, and a 100 percent risk weight could significantly curtail the appetite for these securities among insurance-centric SLHCs. The foregoing provides yet another example as to why these rules are inappropriate for insurance-centric SLHCs, and highlights the need for additional research by the Agencies on the impact of these rules to insurance-centric SLHCs.

E. The Proposed Rules do not appropriately consider the risks of policy loans

The Proposed Rules provide that a 20 percent risk weighting must be assigned to a policy loan, with which Nationwide disagrees and believes that a zero percent risk weighting is

[42] Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies, 77 Fed. Reg. 21,637, 21,661 (Apr. 11, 2012).

[43] 77 Fed. Reg. at 52888, 52898 (Aug. 30, 2012) (emphasis added).

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more appropriate. The definition of a policy loan is a loan to policyholders under the provisions of an insurance contract that is secured by the cash surrender value or collateral assignment of the related policy or contract. This would include: (1) a cash loan, including a loan resulting from early payment or accelerated benefits, on an insurance contract when the terms of the contract specify that the payment is a policy loan secured by the policy; and (2) an automatic premium loan, which is a loan made in accordance with policy provisions which provide that delinquent premium payments are automatically paid from the cash value at the end of the established grace period for premium payments.[44]

The Board's rationale for the 20 percent risk weighting is that it is similar to the treatment of cash-secured loans, which the Board states is appropriate due to the fact that, should a borrower default, the resulting loss to the insurance company is mitigated by the right to access the cash surrender value or collateral assignment of the related policy.[45] However, the Standardized Approach NPR provides that cash secured loans will be assigned a zero percent risk weight. We believe that policy loans should be afforded the same zero percent risk weighting because insurance company policies that allow for policy loans will typically include setoff rights that allow the insurers to net the policy loan's principal and interest payments against the policy's death benefit or cash surrender value in the event of default. Thus, like a cash-secured loan, the right to access the death benefit or cash surrender value offsets the risk of default. For these reasons, we believe a policy loan should similarly be afforded a zero percent risk weight.

F. The tier 2 capital eligibility criteria should be clarified to account for surplus notes issued by insurance companies

The Proposed Rules provide that surplus notes do not meet the eligibility criteria in the Basel III NPR for treatment as tier 1 capital; however, they could be eligible for inclusion in tier 2 capital provided the notes meet the proposed tier 2 capital eligibility criteria.[46] The Basel III NPR sets forth a number of criteria to qualify for tier 2 capital treatment, including but not limited the need for the banking organization to have received prior approval of the agency to exercise a call option on the instrument.

Nationwide believes that surplus notes issued by insurance companies should generally meet the tier 2 capital criteria. However, we wish to point out that surplus notes issued by insurance companies by their terms require approval from the applicable insurance regulator for any payment or prepayment of principal or interest. We respectfully ask the Agencies to clarify in any final consolidated capital framework applied to insurance-centric SLHCs that surplus notes requiring the approval of the applicable insurance regulator would satisfy the criterion in the Basel III NPR that requires the banking organization to receive prior approval of the agency to exercise a call option on the instrument.

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[44] Id.

[45] Id.

[46] 77 Fed. Reg. 52928 (Aug. 30, 2012).

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Conclusion

For the reasons set forth above, Nationwide strongly believes that the Agencies' Proposed Rules inappropriately apply an undifferentiated, bank-centric capital framework to insurance-centric SLHCs. In addition, we believe that the Proposed Rules fail to adequately and appropriately consider the unique characteristics of insurance-centric SLHCs; fail to recognize that insurance-centric SLHCs have never previously been subject to consolidated, bank-centric capital requirements; and fail to provide any transition period for insurance-centric SLHCs to develop the MIS infrastructure necessary to demonstrate compliance with the Proposed Rules. We thus believe that the Proposed Rules are contrary to the letter and spirit of the Dodd-Frank Act and the plain intent of Congress to preserve the thrift charter as a source of personal and household credit, end "too big to fail" and foster financial stability. We respectfully urge the Agencies to develop a consolidated capital framework for insurance-centric SLHCs that takes into consideration the various substantial concerns we have addressed in these comments.

As always, we appreciate the dialogue and look forward to further opportunities to comment.

Very truly yours,

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Appendix A

The following example illustrates how a BHC or SLHC with an operating insurance subsidiary will be required to hold higher capital against the same assets as a BHC or SLHC without an operating insurance subsidiary.

- Company A –SLHC with an insurance operating subsidiary
- Company B – BHC with no insurance operating subsidiary

	Company A	Company B
Assets:	7,000,000	7,000,000
Type:	BBB rated Corp. Bonds	BBB rated Corp. Bonds
RBC After-tax		
C1 (Credit)	59,150	-
C2 (Insurance)	22,590	-
C3 (Interest rate, health, market)	29,180	-
C4 (Business)	7,400	-
Total	118,320	-
Total after Covariance	89,070	-
Authorized Control Level (50%)	44,535	-
Attributable to:		
Credit	25,270	
Interest Rate, Market	9,180	
Total Asset Risk	34,450	
Insurance and Business Risks	10,085	
Risk Weighted Assets	7,000,000	7,000,000
Total Minimum Capital Requirement 8%	560,000	560,000
Total Capital Requirement		
2x Authorized Control Level	89,070	
Attributable to:		
Credit	50,540	-
Interest Rate, Market	18,360	
Total Asset Risk	68,900	
Insurance and Business Risks	20,170	-
Minimum 8% RWA	560,000	560,000
TOTAL	**649,070**	**560,000**
Attributable to Asset Risks	**628,900**	**560,000**
Attributable to Insurance Risks	20,170	-

In the above simplified example, each Company owns a portfolio of BBB rated corporate bonds valued at \$7 million, which are risk-weighted at 100%. Thus, under the Proposed Rules, Company B would be required to hold \$560,000 in Common Equity Tier 1 Capital, Additional Tier 1 Capital, and Tier 2 Capital against these assets to meet the 8% Total RBC ratio. However, Company A, which is required to deduct from Total Capital 200% (or 2x) the subsidiary's authorized control level risk-based capital, would be required to hold \$649,070 (or an additional \$89,070) in Total Capital against the exact same assets.