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Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attn.: Mr. Robert deV. Frierson, Secretary

Re: Amendments to the Capital Plan and Stress Test Rules (Docket No. 1492; RIN 7100-AE 20)

Ladies and Gentlemen:

American International Group, Inc. (AIG) appreciates the opportunity to comment on the notice of proposed rulemaking (Proposed Rule) released by the Board of Governors of the Federal Reserve System (Board) to amend certain aspects of its capital plan rule (section 225.8 of Regulation Y) and stress test rules (subparts B, E, and F of Regulation YY and the Policy Statement on the Scenario Design Framework for Stress Testing).

AIG is a leading international insurance organization serving customers in more than 130 countries and jurisdictions. AIG companies serve commercial, institutional, and individual customers through one of the most extensive worldwide property-casualty networks of any insurer. In addition, AIG companies are leading providers of life insurance and retirement services and mortgage insurance in the United States.

We take a strong interest in the Proposed Rule and the development of enhanced prudential standards as mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act.[1] Although as a nonbank systemically-important financial institution supervised by the Board (Nonbank SIFI) AIG is not presently subject to the capital plan and stress test rules that the Proposed Rule would amend, we recognize that we will be subject to such rules in due course after becoming subject to minimum regulatory capital requirements. As an internal risk and capital management tool, AIG already performs internal stress tests and capital planning exercises that are designed to capture the important

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111–203, 124 Stat. 1376 (2010).

aspects of our insurance business and the expectations of our federal supervisor, the Federal Reserve Bank of New York. We follow with interest, and support, the Board's intention, stated in an earlier rulemaking establishing final enhanced prudential standards for bank holding companies (BHCs) and foreign banking organizations (Enhanced Prudential Standards Rule for BHCs), "to assess the business model, capital structure, and risk profile of [Nonbank SIFIs] to determine how the proposed enhanced prudential standards should apply, and if appropriate, . . . tailor application of the standards" [2] to Nonbank SIFIs. Such tailoring is essential to create capital planning and stress test exercises that are useful both to the Board charged with regulating Nonbank SIFIs and to the executives of those companies who manage them. We also support the Board for recognizing in the Proposed Rule the need to adapt capital plan and stress test rules (so far designed primarily with BHCs in mind) to the realities of the specific businesses of Nonbank SIFIs and for reserving to itself "additional flexibility . . . to tailor the stress test rules to nonbank financial companies."[3]

AIG offers specific comments on the following aspects of the Proposed Rule:

1. Definition of a "BHC stress scenario"

AIG agrees with the Board's proposal to add the new defined term "BHC stress scenario" to the capital plan rule. As noted in the Proposed Rule, this formalization signifies the emerging importance of performing scenarios tailored to a company's specific vulnerabilities, operations and business risk profile.

An evolution toward more tailored, company-specific scenarios will be constructive if it introduces into the capital and stress test exercises more of the realities actually faced by regulated nonbank financial companies, such as those involved in the insurance business. It will be particularly salutary for efforts to regulate global, diversified insurance firms, which are exposed to risk factors not represented by the primarily financial-related risks captured in the Board's scenarios designed for BHCs. We support the Board's increasing emphasis on stress scenarios designed by companies to reflect the institution's specific diversity of business activities and risk profiles. The application of tailored scenarios will aid supervisors by revealing risks unique to each company that scenarios designed for BHCs would not. Tailored scenarios also promise to be of great utility to the financial firms subject to stress testing and their senior management. Running stress scenarios specifically designed to reflect a

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[2] Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 79 Fed. Reg. 17240, 17245 (March 27, 2014).

[3] Amendments to the Capital Plan and Stress Test Rules, 79 Fed. Reg. 37420, 37423 (July 1, 2014).

company's own unique risk factors provides more relevant and useful management information.

To provide this additional value, however, the stress scenarios must be tailored effectively. The Proposed Rule states that "an appropriately tailored scenario is generally expected to result in an impact to projected pre-tax net income that is at least as severe as the results of the bank holding company's company run stress test under the Board's severely adverse scenario."[4] The Proposed Rule goes on to say, however, that a stress scenario will not be deemed appropriate only because it produces capital ratios that are lower than those produced under the Board's severely adverse scenario. The Board would assess severity both in terms of stress test outcomes (*i.e.*, degree of negative impact on regulatory capital ratios) as well as the overall design of the scenario itself, which is expected to capture the firm's "idiosyncratic positions and activities"[5] and the attendant risks. We agree that scenario design is an important aspect of assessing cumulative severity, and believe it is important for the Board to clarify the criteria and considerations that it will bring to bear in this assessment.

In particular, it is critical that the Board recognize the important role that risk factor diversification plays in reducing potential cumulative losses in a stress scenario. For example, the natural catastrophe risk inherent in aspects of AIG's Property Casualty (PC) business is unlikely to manifest concurrently with a severe adverse reserve development (*e.g.*, asbestos-related) and a financial crisis, given the limited dependencies among these underlying risk factors. An internal scenario that does not recognize these limitations in tail dependencies and, instead, takes only a simple additive approach to risk factors with low dependencies, would by definition increase cumulative severity, but at the expense of plausibility.

Recognizing the effects of risk factor diversification within internal scenarios is an essential part of appropriate "tailoring" and advances one of the stated objectives of the Proposed Rule, namely to have each firm that is subject to the capital plan and stress test rules "design its own stress scenario that is appropriate to the company's business model and portfolios."[6] Diversification is central to AIG's business model, which is based on providing customers with an array of PC, Life and Retirement, and Mortgage Insurance products supported by an investment portfolio whose financial risks, in many cases, have limited dependencies with the underwriting risks in our insurance business.

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[4] *Id.* at 37425.
[5] *Id.*
[6] *Id.* at 37424.

Permitting internal scenarios to recognize the low dependencies between certain financial and non-financial risk factors would help promote the business relevance and management utility of stress test results. In addition, such recognition would create a prudential incentive for firms to limit concentration risks and to more finely assess the potential interplay of key risk factors in a stress scenario. More broadly, recognition of risk factor diversification aligns with the appropriate evolution of stress testing as a more idiosyncratic exercise that is tailored to reflect the unique risk and business profile of each firm. The meaningful tailoring of scenarios, which for insurance companies includes the recognition of limited dependencies among certain risks, will further increase the relevance of stress testing to all stakeholders, including participating firms, the Board, and market participants.

2. Stress Run Period

Pursuant to the Enhanced Prudential Standards Rule for BHCs, participating companies perform annual company-run stress tests using data of a given date (eventually, after transition under the Proposed Rule, to be December 31 and June 30, for the two respective cycles) over a run period of three months and five days. We wish to point out that when an insurance company closes its books at quarter end, unlike a banking entity, it must perform a valuation of its liabilities, which involves actuarial judgment and review and generally adds several weeks to the process. Insurance companies routinely release quarterly earnings results well after banks do. We respectfully ask that, in light of this fact, the Board allow itself flexibility in setting the relevant deadline, so that financial companies concentrated in the insurance business that are participating in this process are not put at a disadvantage.

We also would like to express our support for the proposed movement in timeframe of the stress test cycles to be based on year-end and mid-year financial reporting periods. This change in timeframe would help to alleviate resource constraints, given other financial reporting requirements that overlap with the current timeframe.

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AIG appreciates the opportunity to comment on the Proposed Rule. We would be pleased to answer any questions you may have regarding our submission.

Respectfully submitted,

Kim Olson