Stephen McManus, CPCU®, CLU®, ChFC®
Senior Vice President and General Counsel

One State Farm Plaza
Bloomington, Illinois 61710-0001

September 16, 2016

Robert deV. Frierson
Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave., NW.
Washington, DC 20551
Via Email: regs.comments@federalreserve.gov

Re: Capital Requirements for Supervised Institutions Significantly Engaged in Insurance Activities, Docket No. R-1539, RIN 7100 AE 53

Dear Mr. Frierson:

State Farm Mutual® Automobile Insurance Company ("State Farm Mutual"), a mutual insurance company and a savings and loan holding company ("SLHC"), appreciates the opportunity to submit these comments on the advance notice of proposed rulemaking ("ANPR") regarding approaches to regulatory capital requirements for supervised institutions engaged in insurance activities, and nonbank financial companies that the Financial Stability Oversight Council ("FSOC") has determined will be supervised by the Board of Governors of the Federal Reserve System ("Board").

The State Farm Mutual group is principally engaged in the business of insurance and is primarily focused on personal lines of insurance with the vast majority of its customers being individuals, families, and small businesses. State Farm Mutual is the leading writer of automobile insurance in the country and the State Farm Mutual group also includes the leading writers of homeowners and individual ordinary life insurance. The State Farm Mutual group includes State Farm Bank, F.S.B., ("the Thrift") and State Farm Mutual is a "grandfathered" unitary SLHC, as defined in section 10(c)(9)(C) of the Home Owners' Loan Act ("HOLA").

State Farm Mutual is a fully regulated insurance company. From the consumer's perspective, the ability to obtain a diverse range of financial services from State Farm insurance companies and the Thrift provides important benefits. These include familiarity with State Farm's products, financial strength, convenience, more consistent and personalized service, account-maintenance efficiencies and one stop service for many of their financial needs. The Thrift also injects competition into the market for banking products and services. Notwithstanding these benefits, the Thrift remains a relatively modest part of the State Farm Mutual group's total operations. Almost 92% of the total assets of the group are related to insurance operations and the insurance operations account for 99% of the group's total revenues. In addition, and important to the issue of capital standards for the parent companies of thrift institutions, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DFA") did not change the substantial limitations on permissible activities of grandfathered thrifts. Indeed, the Qualified Thrift Lender Test, historically intended as a key governor on the activities of these thrifts, continues to limit activities of the subsidiary thrifts and does not permit such activities as commercial lending, real estate development loans or similar activities as are engaged in by full service commercial banks.

This cover letter provides State Farm Mutual's general thoughts and observations concerning the ANPR with more detailed discussion provided in responses to the questions posed in the ANPR. Both the cover letter and responses emphasize State Farm Mutual's views on how an effective capital framework could be structured to recognize the principles of state regulation of insurance including utilization of existing state-based insurance regulatory tools, the business model of insurance, and federal regulation of thrifts and thrift holding companies. State Farm Mutual's principal thoughts can be summarized as follows:

- State Farm Mutual commends the Board for its conscientious and deliberative efforts to tailor capital rules for the business of insurance and its willingness to be flexible in recognizing the many distinctions between different insurers under its supervision.
- State Farm Mutual believes strong and effective capital and solvency regulation is essential to maintaining the integrity of well-functioning markets.
- The proposed Building Block Approach (BBA) is an effective mechanism for leveraging existing capital and other related requirements, especially for state-regulated insurance entities.
- The BBA reflects statutory directives and congressional intent to defer to state insurance law to the greatest extent practical for institutions significantly engaged in insurance activities.
- The BBA allows the Board to follow congressional intent and adopt a "single building block" ("SBB") for SLHCs where the holding company parent is regulated under state insurance laws.
- The Board should also look to the abundance of state insurance laws and other supervisory regulations, particularly on matters relating to risk assessment and stress testing.
- The Board should reject any "consolidated" approach that suggests capital is freely fungible across legal entities within an insurance group and which ignores the well-established legal separation of such legal entities.

State Farm Mutual Commends the Board for Seeking a Tailored Approach to the Insurance Business Model Consistent with Congressional Intent to Preserve State Law

First and foremost, State Farm Mutual applauds the Board for its conscientious and deliberative efforts to develop an appropriate and effective capital framework for insurance companies under its supervision. As the Board has expressed numerous times, the ultimate goal of this endeavor is not to simply promulgate a capital rule as quickly as possible, but to get it right and avoid unnecessary disruption to well-functioning state-regulated insurance markets. The significant time, effort, and resources the Board and its staff dedicated to meeting this objective are reflected in this thoughtful ANPR and is genuinely appreciated.

In particular, the proposed BBA advanced by the Board, can satisfy most, if not all, of its regulatory objectives through its leveraging of existing and proven insurance financial regulatory frameworks for capital, especially the Risk Based Capital regime ("insurance RBC") established by the states through the National Association of Insurance Commissioners ("NAIC"). This tailored capital approach, including the use of existing books and records, and which does not compromise the sound and prudential supervision of insurance companies, has salutary effects on controlling regulatory costs and burdens - benefits that well-serve State Farm customers while recognizing the legal entity regulation of insurance. Indeed, State Farm Mutual urges the Board to seek further tailoring opportunities that build upon this solid foundation, and utilize more components of the existing and comprehensive U.S. insurance capital and solvency framework, including explicit recognition and use of the Own Risk and Solvency Assessment ("ORSA") requirement in lieu of any stress testing requirements contemplated by the Board for SLHCs.

State Farm Mutual also strongly supports Congress's and the ANPR's fundamental goal of promoting capital adequacy for regulated financial institutions. At the same time, however, State Farm Mutual believes that government regulation of company capital must be tailored to the business model and risks of the supervised company. Finally, capital rules should be both sensible and not unnecessarily burdensome. Regulatory requirements failing to meet these objectives, particularly those mismatched with business and economic realities that create duplicative and conflicting regulatory requirements, or those that do not comport with legal entity regulation, do a tremendous disservice to all stakeholders involved.

Nowhere is the need for tailored supervision more evident than in the development of rules or standards governing regulated insurance companies coming under Board supervision. In enacting the DFA Congress fundamentally altered federal oversight for all SLHCs, including those engaged extensively in the business of insurance. It is also true that certain activities of an insurance company at the center of the financial crisis meant that the supervision and regulation of insurance companies did not escape the bounds of congressional attention, concern, and reach. Nevertheless, Congress understood that insurance company operations are fundamentally different than banks. After several months of careful deliberation, Congress affirmatively determined that McCarran-Ferguson should continue as the controlling federal law and that state regulation of insurance remains the paramount regulatory structure for the industry—even for federally-supervised insurers. To the extent DFA suggested any ambiguity concerning this intent and the ability of the Board to defer to state law governing insurers, Congress passed, on a bipartisan basis without any objection, the Insurance Capital Standards Clarification Act of 2014 (the "Clarification Act"), the only substantive amendment to the DFA in the first four years since its enactment.[1]

[1] Public Law No: 113-279

Congressional Intent Concerning SLHCs and Top-Tier Insurance Companies

The case for deferring to state regulation in accordance with congressional intent is most clear and compelling for SLHCs where the holding company itself is a state-regulated insurance entity. Unlike systemically important financial institutions ("SIFIs"), where Congress mandated the adoption of capital rules for such companies, HOLA, which governs thrifts, makes the adoption of capital rules discretionary for SLHCs. The only other federal statute requiring minimum capital rules for such holding companies is Section 171 of the DFA as originally enacted. Although many believed Section 171 authorized the Board to utilize existing state risk-based capital standards to satisfy this minimum capital requirement, any doubt on this subject was addressed by the subsequent enactment of the Clarification Act, giving the Board explicit authority to treat insurance companies differently, including deferring to the existing state regulatory capital framework.

Congressional intent on this matter was further amplified through a provision in the Clarification Act relating to the accounting requirements governing certain SLHCs. Specifically, Congress prohibited the Board from requiring SLHCs who prepare financial statements using only Statutory Accounting Principles ("SAP") from preparing those statements utilizing Generally Accepted Accounting Principles. Inclusion of this provision had three impacts. First, it avoided imposing an undue burden and hundreds of millions of dollars of additional costs for several insurance companies for a negligible, if any, supervisory benefit. Second, it reflected Congress's unambiguous decision to validate the sufficiency of such SAP statements and the underlying state-based insurance RBC requirements for which they are utilized in satisfying any federally established capital standards. Finally, and related to the second impact, it allowed such SAP statements to be utilized for supervisory purposes where the Board has traditionally relied upon consolidated financial statements, particularly where insurance RBC can serve as a proxy for "consolidation" as this term has been traditionally applied by the Board. In fact, the accounting provision makes little sense without such an understanding; otherwise SAP and state-based requirements tied to SAP would serve no regulatory purpose. Indeed, it appears that reliance on SAP statements and the congressional directive on the matter provides the very foundation of the Board's BBA (discussed in more detail below).

Taken to its natural conclusion, the Board should view a top-tier insurance SLHC as a SBB within its BBA, where the capital requirement of a state-regulated top-tier insurance entity is the only block needed. Nothing in this single block approach rejects the notion that federal authority over insurance-based SLHCs is an essential component of Congress's statutory scheme and should be abandoned. Instead, it fully recognizes and incorporates Congress's decision to rely on and incorporate existing functional regulation to the greatest extent practical.[2]

[2] In similar fashion, even where the top-tier company is not an insurer, as discussed more fully later in the cover letter, State Farm Mutual believes it is appropriate for the Board to utilize the highest level insurance blocks within a group wherever possible when the group is primarily an insurance operation. For example, if a non-insurer sits at the top of the house of an SLHC and three principal subsidiaries that are regulated insurance companies with five insurance companies under each one, the Board should look solely to aggregating the capital requirements of the top three blocks as opposed to looking at the requirements of all eighteen subsidiaries.

In sum, in enacting the DFA, Congress was explicit in preserving the thrift charter and allowing diversified types of business organizations to continue owning a thrift. It is also clear and unmistakable that Congress had a positive view of state insurance law, including the recognition and continued use of SAP and insurance-based capital measures for federal supervisory purposes. As such, consistent with all applicable statutes and congressional intent, where the SLHC is itself a regulated insurance entity, there is simply no need for the Board to re-invent the wheel and establish a second additional layer of regulatory capital oversight regardless of whether that is the BBA for SLHCs that are regulated insurers or the SBB approach for SLHCs that are regulated top-tier insurers.[3] In these circumstances, the Board has clear authority to defer to and fully incorporate existing state-based insurance RBC framework and capital requirements for such companies. The Board should only seek to establish a second additional regulatory capital framework where it makes a determination that the existing state regulatory capital framework is inadequate for federal supervisory purposes.

The Building Block Approach is Effective for all Types of Insurers, Allows for Single Building Block Supervision, and Provides Greater Opportunities to Leverage Existing State Laws and Regulations

Not all federally supervised companies are structured as SLHCs with a top-tier regulated insurance entity. State Farm Mutual acknowledges that these circumstances may introduce more complexity into the rulemaking process. Nonetheless, since enactment of the DFA, the insurance industry has consistently articulated the stark differences between insurers and banks and how the traditional regulation of bank holding companies predominantly engaged in banking-related activities was wholly inappropriate for a company significantly engaged in the business of insurance. There now appears to be little disagreement that even where a non-insurance company is the holding company parent of insurance operations with activities supported with a diverse range of insurer investments, state-established insurance RBC most effectively captures the risks associated with insurance operations and investments and does so in a manner that is tailored to the business models and asset utilization strategies of insurance-based companies. As such, and wholly consistent with the discussion and suggestions above for top-tier insurance SLHCs, State Farm Mutual believes the Board's conceptual approach on the BBA represents an effective approach for measuring capital needs for all types of insurance companies it supervises. In essence, the proposed BBA recognizes both: 1) that differences in financial institutions require distinct regulatory approaches; and 2) existing state-based insurance RBC and related requirements can be effectively leveraged for federal supervision of insurer capital.

The standardized approach of the BBA can capture all material risks impacting differently regulated groups while striking a thoughtful balance between risk sensitivity and simplicity. As the Board noted, it is a standardized approach utilizing existing U.S. accounting principles for U.S. entities that is intended to result in relatively low additional regulatory cost and burden. It should be able to be implemented in an expeditious manner as it leverages existing supervisory capital regimes. It is well tailored to the risks faced by SLHCs both in the business segments and jurisdictions in which they operate. Importantly, it is comprehensive and accounts for all material risks. Such a capital framework can be applied to both SLHCs and SIFIs.

[3] See the State Farm Mutual 2012 comment letter https://www.regulations.gov/document?D=OCC-2012-0009-0744.

The BBA can indeed satisfy most, if not all, of the Board's regulatory objectives with minimal disruption to insurers by leveraging existing and proven insurance financial regulatory frameworks for capital, especially the insurance RBC. State Farm Mutual is keenly aware of the regulatory costs and burdens of multiple overlapping supervisory frameworks and the impact that has on its customers. Consequently, this tailored capital approach, including the use of existing books and records, which doesn't compromise sound and prudential supervision of insurance companies, has very positive implications for controlling regulatory costs and burdens - benefits that well-serve customers. It also has the additional benefit of ongoing improvements made in the individual regimes that automatically become part of the BBA. In sum, the Board's use of the existing regulatory capital frameworks that rely on the underlying financial reporting systems already in place works to the benefit of companies, supervisors, and customers.

It also should be noted, insurance RBC is calculated only annually from statutory annual financial statements and relies on annual and historical results to calculate underwriting risk charges. State Farm Mutual strongly believes that performing the BBA calculation on an annual basis, particularly when considered in combination with other reporting and the Board's continuous monitoring program, would not be detrimental to the Board's ability to perform its oversight functions.

Finally, it is worth highlighting that over the last year, State Farm Mutual has been a participant in the American Council of Life Insurers' ("ACLI") effort to develop the Aggregation and Calibration Approach ("A&C") to calculate a group capital measurement. The BBA appears to be very similar to the A&C and, based on State Farm Mutual's experience with the A&C, State Farm Mutual believes BBA would work well for SLHCs and could also be applied to insurance SIFIs.

Although the BBA as proposed is an appropriate framework for all types of federally regulated or supervised insurance entities, as outlined in the discussion above concerning top-tier insurance SLHCs, the BBA framework is also fully amenable to incorporating a SBB approach for any SLHC that has a licensed insurance entity as the top-tier parent of the group. The SBB would apply to all facets of insurance company operations -- from capital to accounting -- and is sufficient to satisfy any federal regulatory requirements for holding companies with a top-tier regulated insurer. For instance, the solvency ratio developed by the A&C for the State Farm Mutual group was not significantly different than State Farm Mutual's legal entity insurance RBC ratio. This analysis gives the Board further assurance that reliance solely upon insurance RBC measurements would also be sufficient to meet the supervisory goals of the Board. Again, since the BBA recognizes the validity and adequacy of existing functional multi-faceted regulation to which the SLHC or its affiliates and/or subsidiaries are already subject, it is wholly within the Board's discretion to simply defer to the existing insurance RBC framework and capital requirements for such SLHCs.

Using State Farm Mutual as an example to illustrate the efficacy of the SBB, all parts of the State Farm Mutual group are comprehensively governed and all of State Farm Mutual's subsidiaries are subject to holding company system examination by the Illinois Department of Insurance (the "Illinois Department") and other applicable domiciliary state insurance departments. There is no material aspect of the State Farm business that is not currently subject to comprehensive prudential oversight by state regulators. Every investment by State Farm Mutual and its insurance subsidiaries must be made in accordance with state law and is subject to state review. Moreover, the combination of direct state regulation of specific insurance operations and investments and insurance holding company laws means every area and aspect of State Farm Mutual's business is subject to close regulatory scrutiny. Under state law, particularly for top tier regulated insurers, there are simply no "regulatory shadows" within which any aspect of the enterprise's operations could hide. The operations of the enterprise are transparent to regulators - federal and state.

Any Perceived Weaknesses of the BBA can be Mitigated and are Overwhelmingly Outweighed by the Benefits

State Farm Mutual notes that the Board has articulated some perceived weaknesses in the BBA. However, those perceived weaknesses can be mitigated by the rules established to implement it. For groups where the top-tier parent is itself regulated under state insurance law, such as State Farm Mutual, with no outside ownership, the parent’s capital can be considered “consolidated” because as the owner of all subsidiaries the equity value of all subsidiaries is included in the parent’s capital pursuant to statutory accounting principles[4]. All activities and investments of the parent, including any subsidiary insurers, are brought into the parent’s insurance RBC calculation. And while it is clear that certain aggregation adjustments within the BBA may be necessary to adjust for inter-affiliate transactions, such as capital invested in a subsidiary by the parent, the existing insurance RBC formula already incorporates these adjustments. For other potential adjustments, affiliate holdings and transactions are clearly identified in statutory financial statements making them readily identifiable for adjustment. For other organization structures, the BBA rules can make clear that capital should only be counted once as available capital and that certain transactions (e.g. surplus notes or intercompany loans) should not be risk charged twice to develop required capital. This is supported by the fact that only relatively minor, straight forward adjustments were required by State Farm Mutual in its A&C testing.

Furthermore, as to the potential for regulatory arbitrage, for the State Farm Mutual group, with the parent fully regulated under state insurance laws, all aspects of the group are subject to insurance regulatory supervision. The state-based insurance holding company statutes and regulations require that all material affiliate transactions within the group receive prior regulatory review and are subject to disapproval. Consequently, the transfer of funds between affiliates and jurisdictions would be subject to regulatory scrutiny. In addition, while many of the affiliates and subsidiaries are themselves insurance or other regulated entities, their equity values are held as assets of the parent and thereby are subject to insurance regulatory examination and review. Therefore, for State Farm Mutual, the entirety of the group’s operations are regulated by state insurance regulators. With the Thrift, also regulated by the OCC, the Board should take comfort that State Farm Mutual is already fully regulated. For other organization structures, all transactions with U.S. regulated insurers and their subsidiaries would be similarly regulated. Consequently, any effort to gain a regulatory advantage would be unavailing.

To the concern that potential stress-testing would need to rely on legal entity level stress tests, State Farm Mutual would note that any stress testing regulations promulgated by the Board for SLHCs can rely on existing insurance ORSA requirements. These are performed on a group basis by State Farm Mutual and can be effectively utilized for federal supervisory purposes.

[4] Note that the State Farm Mutual group does not utilize consolidated financial statements nor consolidated group capital when determining a legal entity’s financial needs or premium rating needs and the insurance RBC does not consider a legal entity’s capital based on overall group capital.

Given the extensive benefits of the BBA described above, any of the Board's concerns with the BBA can be sufficiently mitigated such that it can proceed with the BBA as generally proposed in the ANPR should the Board deem it necessary.

Leveraging the BBA Foundation for Additional Areas of Insurance Supervision

Closely tied to capital adequacy is risk assessment and stress testing. Of particular note, there is significant opportunity for the Board to leverage the ORSA requirements in lieu of establishing a separate stand-alone stress testing requirement, should the Board ever contemplate such a need for SLHCs significantly engaged in the business of insurance. As noted above, State Farm Mutual's ORSA provides a comprehensive review of its enterprise risk management framework, risk identification, measurement and management processes, economic capital modeling, stress testing, and capital adequacy assessment. State Farm Mutual's ORSA is prepared on a group basis that includes the impact of intercompany risk transfer, diversification or other intra-group transfers which should alleviate the Board's concerns with aggregating legal entity stress tests. State Farm Mutual's ORSA can be effectively utilized for federal supervisory purposes. Importantly, any approach the Board utilizes to monitor capital and solvency of an SLHC should continue to recognize the legal entities within the group and the explicit restrictions, which the Board itself has previously recognized, on the transferability of funds between legal entities within a group. For regulated insurance groups, capital is not freely transferrable across different entities within the group and any group capital measurement should explicitly recognize this reality.

In short, outright deference to, as well as, additional leveraging of existing insurance regulatory solvency tools are fully consistent with the objectives and underpinnings of the DFA and the proposed BBA. The BBA should provide sufficient flexibility to make appropriate accommodations for regulated insurance SLHCs and, if necessary, prove effective for federal supervisory purposes.

Consolidated Approach Could Undermine Longstanding Insurance Regulatory Framework

State Farm Mutual is concerned with the fundamental premise underlying any form of group capital requirement, namely, that capital is freely fungible between parent, subsidiaries and affiliates of regulated groups. As the Board is aware, U.S. insurance regulation is legal entity focused with strict oversight and required regulatory review of all company proposed material inter-affiliate transactions. The solvency framework, indeed, utilizes a "Windows and Walls" philosophy wherein the "Walls" represent the strict limitations on movement of capital between regulated insurers and other members within the group. In addition, history has revealed the difficulties in extracting and moving affiliated capital from one international jurisdiction to another in times of financial stress within a group.

One cannot fault regulators for taking actions to protect the policyholders in their jurisdictions by preventing capital withdrawals from their regulated companies for the benefit of stakeholders of affiliate companies in other jurisdictions. Conversely, companies cannot be compelled to make additional investments in affiliated companies that potentially could put their own policyholders at greater risk. Policyholders in one entity should not be called upon to subsidize policyholders in another entity. This highlights the underlying premise and benefit of legal entity regulation - each entity must stand on its own. Indeed, the capital requirements of each state requires that any legally distinct insurer be fully capitalized on its own merits.

Capital is only fungible when: 1) it exists within a related group, and 2) the company can be compelled to transfer it between affiliates. Without such characteristics, capital is not truly fungible and therefore any measure of group capital in such circumstances has limited regulatory value. A measure of group capital can be helpful in ongoing monitoring and assessment of the financial strength of a group of companies but such a measure should not be utilized as a strict requirement or a measure of an individual legal entity's capital position. A group regulator's actions are very limited and ultimate corrective action must be addressed by the local regulator with statutory authority to act upon the individual group members.

For these reasons, State Farm Mutual is concerned that the Consolidated Approach ("CA") may contribute to reliance on such a flawed premise and, therefore, has the potential for dangerously advancing the notion that capital is freely fungible within an insurance group, thereby undermining the longstanding legal-entity framework of insurance that serves as the very foundation of any effective rule tailored to the insurance business model.

Conclusion

State Farm Mutual appreciates the Board's response to Congressional action and intent governing insurance companies under Board supervision and the Board's recognition, through the ANPR proposal, of the differences between banks and insurance companies. The proposed leveraging of existing insurance regulatory frameworks will have important benefits to State Farm customers through cost effective regulations.

The BBA provides an effective framework for measuring capital within an SLHC significantly engaged in insurance activities. Consistent with all governing statutes and congressional intent, the Board should treat a top-tier state-regulated insurance SLHC as a SBB and defer to and incorporate state rules for such companies. The Board should expand its reliance on other existing insurance regulation as it considers the applicability of its existing banking supervisory tools to the insurance SLHCs it now regulates. Finally, the CA contemplated by the ANPR lends support to the dangerous notion that capital is freely fungible within an insurance group, undermining the well-established legal-entity framework of insurance that is the foundation of any effective rule tailored to the insurance business model.

State Farm Mutual's detailed answers to the Board's questions in the ANPR follow. State Farm Mutual appreciates the opportunity to comment on the Board's proposal. Please feel free to contact me if you should have any questions.

Very truly yours,

Stephen McManus

Stephen McManus
Senior Vice President and General Counsel
State Farm Mutual Automobile Insurance Company

State Farm Mutual's Response to ANPR Questions:

In enacting the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DFA"), Congress was explicit in seeking to preserve the unique consumer-oriented focus of the thrift charter and allowing diversified types of business organizations to continue owning a thrift. Congress clearly intended to give the Board flexibility and discretion in developing capital requirements for SLHCs whose primary operation is insurance. It is also clear and unmistakable that Congress sought to preserve state regulation of insurance to the greatest extent possible, including the recognition and the continued use of Statutory Accounting Principles ("SAP") and insurance-based capital measures. Consistent with Congressional intent and statutory requirements, State Farm Mutual has long-contended that where the SLHC itself is a regulated insurance company, there is no need for the Board to re-invent the wheel. In these circumstances, the Board's decision to establish capital rules is entirely discretionary. State Farm Mutual believes it is wholly within the Board's authority to defer to the existing state-based RBC framework and capital requirements for such companies unless it makes an affirmative determination that such state requirements are inadequate for federal supervisory purposes. In the case of State Farm Mutual, this would imply utilization solely of State Farm Mutual's insurance RBC, without the need for further, additional capital measurement.

Given the robust nature of the insurance regulatory paradigm in place, State Farm Mutual believes that reliance on insurance based tools and measures gives the Board the data and information needed to assure itself of the capital adequacy of its supervised entities which are regulated by state insurance regulators and subject to state based capital requirements.

Framework Options Questions 1 - 5:

Question 1. Are these identified considerations appropriate? Are there other considerations the Board should incorporate in its evaluation of capital frameworks for supervised institutions significantly engaged in insurance activities?

State Farm Mutual applauds the Board's efforts of identifying the considerations for a capital framework appropriate for institutions significantly engaged in insurance activities and regulated by the Board as SLHCs or SIFIs. While not stated as such, the Board's proposals appear to leverage significantly the existing, time tested, and comprehensive solvency framework utilized by U.S. insurance regulators. The ability to further leverage these insurance-based regulatory tools (e.g. insurance-based Own Risk and Solvency Assessment ("ORSA") for stress-testing) is another important consideration to avoid costly duplication of regulatory efforts. Collaboration across regulator groups can leverage the expertise and knowledge that each applicable regulator has of the regulated entity, as well as broadening the understanding of unique industry characteristics. The proposed conceptual framework establishes the foundation for such future collaboration.

Question 2. Should the same capital framework apply to all supervised insurance institutions?

Consideration of a group's risk profile is relevant when attempting to apply a capital framework to a supervised insurance institution. Tailoring the framework based on the risk exposures of the individual regulated firms will generate a better result. State Farm Mutual recognizes that with more complex risk profiles (e.g. multiple regulatory regimes, geographic disparity of markets and products, etc.) the burdens associated with the use of a more tailored framework could outweigh the benefits. However, for many of the supervised insurance institutions regulated as SLHCs with less complex risk profiles, regardless of size, the same framework should produce the desired outcomes while meeting the regulatory needs set out by the Board.

Question 3. What criteria should the Board use to determine whether a supervised insurance institution should be subject to regulatory capital rules tailored to the business of insurance?

The Board should develop criteria for establishing thresholds for capital requirements that contains the appropriate flexibility to account for differences between corporate structures. Specifically, the flexibility should account for the different regulatory structures for insurance entities that are based on the individual legal entity. It may be appropriate to include criteria from Regulation Q so long as such criteria are an appropriate barometer for all assets being measured or are applied only to those assets to which it is relevant.

An insurance capital framework is appropriate for any holding company that is also a regulated insurance company itself or which is significantly engaged in the business of insurance. State Farm Mutual believes that it is imperative than any framework maintain the integrity of the legal entity regulation of insurance companies and avoid regulatory requirements that compromise or call into question this longstanding and successful approach. Recognizing the many differences in companies under the Board's supervision, the ultimate framework should provide appropriate flexibility to account for differences between corporate structures and specifically, the historical and current U.S. regulatory structure for insurance entities which is based on the individual legal entity and the understanding that capital across an insurance group is not held for the sole purpose of being readily fungible across affiliated entities.

Question 4. If multiple capital frameworks are used, what criteria should be used to determine whether a supervised insurance institution should be subject to each framework?

Notwithstanding State Farm Mutual's belief that U.S. SLHCs with top tier regulated insurers do not need to be subject to any Board required capital framework (i.e. simply defer to the existing insurance RBC framework and capital requirements for such top-tier insurance SLHCs), State Farm Mutual generally believes it would be appropriate to consider characteristics of the group's risk profile as articulated in the answer to question 2 above. The regulatory goals or rationale for such a framework must be considered as well as the existence of current capital supervision and regulation applied to the supervised entity

For insurance-based SLHCs, the goals of safety and soundness and source of strength can be achieved with a framework based on existing state insurance capital and solvency regulation such as the proposed BBA.

Question 5. In addition to insurance underwriting activities, what other activities, if any, should be used to determine whether a supervised institution is significantly engaged in insurance activities and should be subject to regulatory capital requirements tailored to the business mix and risk profile of insurance?

While it may be intuitively obvious from the term "insurance underwriting activities", the proposal should require that such activities actually fall under an insurance supervisory regime. A requirement that an entity engaging in such activities actually be licensed as an insurer will ensure an existing and robust supervisory regime is in place which the proposal can then leverage without the need to formulate additional and duplicative regulatory capital requirements.

Building Block Approach Questions 6 – 11:

Question 6. What are the advantages and disadvantages of applying the BBA to the businesses and risks of supervised institutions significantly engaged in insurance activities?

State Farm Mutual agrees with the conclusions reached by the Board as to the strengths of the BBA. State Farm Mutual is especially pleased to see the Board's willingness to utilize the existing insurance regulatory frameworks. This can have significant implications for minimizing additional regulatory costs and burdens. State Farm Mutual believes the Board should consider further leveraging the existing insurance solvency regulatory framework, especially as it relates to stress-testing and solvency assessments through the use of the existing insurance ORSA requirements.

The key advantage of the BBA, as the Board has identified, is that it produces regulatory capital requirements that are tailored to the risks of each distinct jurisdiction and line of business. These capital regulations for the U.S. insurance industry have been well tested over the 20+ years of their existence and have proven to be effective in varying economic conditions. During the 2008 downturn, the rate of insolvencies in the U.S. insurance industry was substantially lower than that of the U.S. banking industry.

Implementation burdens will be relatively small assuming existing insurance rules, reporting schedules and due dates are maintained. State Farm Mutual participated in the ACLI's Aggregation and Calibration ("A&C") project which appears similar to the proposed BBA. The results of State Farm's proof of concept lead to the belief that the BBA approach, to the extent it remains similar to the A&C approach, can be implemented without undue burden in a relatively short timeframe.

As for the perceived weaknesses noted by the Board, State Farm Mutual is confident that they can be mitigated by the rules established to implement the BBA. Nowhere is this more evident than for groups where the top-tier parent SLHC is itself a regulated insurer. For example, for companies like State Farm Mutual, which is a top-tier parent in mutual form with no outside ownership, the parent's capital can be considered "consolidated" as the equity value of all subsidiaries flow into the parent's financials as invested assets and capital. All activities and investments of the parent, including any subsidiary insurers are brought into the parent's insurance RBC. Even where a shell holding company may exist, similar regulatory economies of scale may be achieved if the Board looks primarily to the highest regulated insurance company over a particular subgroup as opposed to looking at each legal entity within the entire SLHC. For example, if a shell holding company served as the top-tier for three wholly-owned and regulated operating insurance subsidiaries with no other subsidiaries, the Board should look towards the capital requirements of those three insurance subsidiaries without having to assess any of the subsidiaries underneath each of those three companies.

Furthermore, the Board's concerns surrounding the potential for regulatory arbitrage are greatly reduced for U.S. regulated insurers, particularly where the top-tier parent is a U.S. regulated insurer as all material transactions within the group receive prior regulatory review and are subject to disapproval by insurance regulators through state based insurance model holding company statutes and regulations enacted by every state.

It is clear that certain aggregation adjustments may be necessary in the BBA to adjust for inter-affiliate transactions such as capital invested in a subsidiary by the parent. The rules can be made clear that capital should only be counted once as available capital and that certain transactions (e.g. surplus notes or intercompany loans) should not be risk charged twice to develop required capital.

State Farm Mutual believes, over time and with proper development, scalars can provide flexibility in fine-tuning the BBA without the need for a redesign of the framework.

Related to the potential for stress-testing applicable to SLHCs, the existing insurance ORSA requirements are performed on a group basis for many companies and can be effectively utilized for federal supervisory purposes.

Question 7. What challenges and benefits do you foresee to the development, implementation, or application of the BBA? To what extent would the BBA utilize existing records, data requirements, and systems, and to what extent would the BBA require additional records, data, or systems? How readily could the BBA's calculations be performed across a supervised institution's subsidiaries and affiliates within and outside of the United States?

Recall that the Home Owners Loan Act ("HOLA") requires the leveraging of existing state reports to the extent possible in this regard.[5] State Farm strongly believes that the existing insurance regulatory framework produces the necessary records and data upon which the Federal Reserve can rely to determine capital adequacy.

It also should be noted insurance RBC is calculated annually from statutory annual financial statements and relies on annual and historical results to calculate underwriting risk charges. State Farm Mutual strongly believes that performing the BBA calculation on an annual basis, particularly when considered in combination with other reporting and the Board's continuous monitoring program, would not be detrimental to the Board's ability to perform its oversight functions. Experience with annual reporting of insurance RBC over the 20+ years of its existence has proven satisfactory.

It is suggested that a materiality threshold be established for determining whether or not a subsidiary or affiliate of a regulated insurer SLHC needs to be dis-aggregated and its required capital calculated separately from its parent. Also, certain non-bank subsidiaries and affiliates of regulated insurers that support insurance operations (e.g. investment subsidiaries, insurance agencies, services providers, etc.), should remain included in their parent's RBC asset risk charges and not be required to be broken out

[5] 12 U.S. C.§1467a(b)(2)(B)

separately with separate required capital calculations performed. The insurance RBC risk charges for these entities are consistent with what would be calculated if these investments or operations were part of the insurers operations directly if not for the separate legal entity organization structure.

The Board may also wish to consider some form of safe harbor for non-U.S. insurance affiliates of domestic insurers to minimize the burden of scaling foreign regimes or restating financials into a compatible regime. Consideration should be given to adopting the option to use a 50% risk charge on the available capital of such subsidiaries or affiliates. This is consistent with the charge for such affiliates in the U.S. insurance RBC formulas.

Question 8. What scalars and adjustments are appropriate to implement the BBA, and make the BBA effective in helping to ensure resiliency of the firm and comparability among firms, while minimizing regulatory burden and incentives and opportunity to evade the requirements?

Scalars are important to calibrate capital requirements of different regulatory regimes. They may be necessary to equalize regulatory stringency or to align regulatory action triggers. They may also be needed where accounting standards and their relationship to capital requirements may differ. For example, it is believed there is significantly more conservatism in the U.S. statutory accounting requirements for life policy reserving than for European IFRS and Solvency II. This results in the capital requirements in the U.S. appearing lower than the capital requirements for Solvency II. Scalars could be used to normalize these differences. The calibration of the scalars may need to change over time but the inherent flexibility they provide is a benefit of the BBA approach as it allows for fine-tuning as experience with the BBA evolves.

Concerns with the use of scalars may be mitigated through cooperation and consultation with the supervisors of the non-U.S. regimes. Collaboration across regulator groups to share understanding and promote cooperation across supervisors may reduce the concerns or uncertainty with the efficacy of foreign capital regimes over time.

Question 9. To what extent is the BBA prone to regulatory arbitrage?

As noted in the answer to question 6, U.S. insurers are subject to uniform state-based holding company statutes and regulations that subject all material inter-affiliate transactions to prior regulatory review and disapproval. This has and will prevent or minimize such arbitrage as it relates to regulated insurance entities within a holding company system as the current regulatory framework is consistent and equitable across U.S. domestic regulatory jurisdictions. For SLHCs where the top-tier parent is a regulated entity (such as State Farm) all material inter-affiliate transactions of the entire group are subject to holding company act reporting and review. For other organization structures, all transactions with U.S. regulated insurers and their subsidiaries would be similarly regulated.

Question 10. Which jurisdictions or capital regimes would pose the greatest challenges to inclusion in the BBA?

From a domestic perspective, insurance entities which are subject to state-based insurance regulatory regimes which assess capital and risk profile at an entity level would easily be included in the BBA. The Board can reasonably place more reliance on other insurance regimes that meet the IAIS Insurance Core Principles (ICP's) as determined by the Financial Sector Assessment Program (FSAP). Particular focus should be placed on ICP 17 and others that set guidance for capital standards.

Question 11. How should the BBA apply to a supervised institution significantly engaged in insurance activity where the ultimate parent company is an insurer that is also regulated by a state insurance regulator? Are there other organizational structures that could present challenges?

Groups where the ultimate parent company is a U.S. regulated insurer present the least amount of challenge. In such cases, the entire operations of the group are subject to insurance regulatory supervision. Insurance RBC for the parent includes the entire group and produces what should be considered an effective measure of required capital on a consolidated basis.[6] While it could be further tailored through the BBA to apply a different required capital to non-insurance regulated subsidiaries or affiliates (e.g. for banking affiliates), wherein a Basel capital standard could be substituted for the insurance RBC asset charge, this would be unnecessary compared to simply utilizing the parent's state-based insurance RBC. Rather, the combination of state-based regulation of insurer investments, state risk-based insurance RBC at the holding company level, and separate regulatory capital charges at the affiliate/subsidiary level (e.g., State Farm Bank must satisfy its own OCC capital requirements) means that the only building block needed is that of the parent.

Beyond capital requirements, the Board can also place greater reliance upon insurance regulators for such groups because the entire operations of the group are subject to the full scope of insurance regulatory solvency tools, including regular risk focused financial condition examinations, CPA audits, SOX-like internal control evaluations, and an ORSA (stress testing) requirement.

More complex organization structures with non-insurer holding company parents may present more challenges to ensure double leveraging of capital is eliminated.

Application of BBA Questions 12 – 22:

Bank capital requirements have historically focused primarily on asset risk whereas insurance capital requirements, in addition to asset risk, also focus on the liability side of the balance sheet and include prospective risk such as future underwriting risk and catastrophe risk. Given insurance regulators' experience and expertise and the proven track record for insurance solvency regulation, the Board would be well served to rely upon the existing insurance solvency regulations as it considers baseline capital requirements for SLHCs significantly engaged in insurance activities.

While the Board serves an important supervisory role, it is clear that the DFA preserved the thrift charter and continues to allow non-bank businesses to operate savings banks with the historical banking limitations placed upon thrifts. Given the diversity of institutions supervised, a one size fits all approach has many shortcomings - which is just one reason Congress directed deferral to state insurance requirements as much as possible. Moreover, Section 171 of the DFA as amended in 2014 unequivocally provides the Board latitude in both deciding whether to impose capital requirements upon insurance based holding companies and the development of such capital standards.

[6] See discussion under Question 38 concerning alternative frameworks.

Question 12. Is the BBA an appropriate framework for insurance depository institution holding companies? How effective is the BBA at achieving the goal of ensuring the safety and soundness of an insurance depository institution holding company?

State Farm Mutual strongly agrees with the initial assessment of the Board that the strengths of the BBA are maximized and its weaknesses minimized if it is applied to SLHCs significantly engaged in insurance activities that are less complex, more U.S. domestic focused and not systemically important. State Farm Mutual further believes that the Board should continue to be mindful of these SLHCs, and the current robust regulatory framework to which they are subject, as Board rule-making continues. The BBA would achieve the regulatory goals of providing for the safety and soundness of the holding company and maintaining its source of strength for its depository institution at a relatively low additional compliance cost. The BBA leverages the significant regulatory responsibilities of insurance regulators which will help moderate compliance costs. It does this, as the Board observes, by providing a standardized, executable approach which utilizes existing U.S. accounting principles. It includes all material risks in a tailored fashion that best measures such risks yet strikes a balance between risk sensitivity and simplicity. It provides an effective framework for measuring capital within a holding company significantly engaged in insurance activities.

Question 13. Would the BBA be appropriate for larger or more complex insurance companies that might in the future acquire a depository institution?

There is nothing inherently flawed with the BBA such that it would be an inappropriate starting point in addressing such a hypothetical situation. For example, the most complex domestic insurance company proposing to become a bank holding company or SLHC would still be subject to a rigorous insurance regulatory regime. Even with more complex organizations with varying business segments and jurisdictions, the BBA appears to meet the needs of safety and soundness and source of strength for insurance centric holding companies. A key benefit of the BBA is its tailored approach to risk measurement.

Question 14. In applying the BBA, what baseline capital requirement should the Board use for insurance entities, banking entities, and unregulated entities?

The insurance RBC calculated Company Action Level is the first regulatory trigger point and, as such, should prove to be an effective point of reference for U.S. insurers. Additional catastrophe risk charges are expected to be implemented in 2017 that will incorporate hurricane and earthquake risk into the P&C insurance RBC formula. These should be included in the measure to assure all material risks are included.

The use of the first regulatory action trigger may provide a calibration point with other regulatory regimes that can be a basis for the scalar determinations. Regulatory stringency variations across regimes would also need to be factored into the scalar determination but the regulatory action triggers should be useful in providing a starting point in those determinations.

Question 15. How should the BBA account for international or state regulator approved variances to accounting rules?

As indicated previously, the BBA leverages existing regulatory capital requirements and supervisory regimes and therefore, caution should be taken before making adjustments to those regimes. It should be noted there are a few inconsistencies within the U.S. insurance framework where a handful of states have what may be considered more conservative requirements than the large majority of states. In these instances, to provide consistent measures the Board should accept adjustments or restatements which result in the use of NAIC promulgated accounting rules in lieu of the more conservative rules of certain states (e.g. New York). For other company specific permitted practices, State Farm Mutual believes these should continue to be used. They have been subject to individual regulatory approval and as such should be considered acceptable without adjustment.

For other international variances, the purposes and context should be considered. For off-shore captives, for example, where the establishment of the captive has the effect of lowering reserve requirements and thus increasing capital, restatement back to U.S. statutory accounting treatment should be required.

One must consider that the capital requirements in the various jurisdictions are based on the accounting standards also in use in those jurisdictions. This consistency is important to maintain.

Question 16. What are the challenges in using financial data under different accounting frameworks? What adjustments and/or eliminations should be made to ensure comparability when aggregating to an institution-wide level?

The use of scalars can help normalize different accounting frameworks especially where it impacts capital requirements. However as previously stated, one must consider that the capital requirements in the various jurisdictions are based on the accounting standards also in use in those jurisdictions. Thus, both the required capital and available capital are developed using the same accounting framework.

Question 17. What approaches or strategies could the Board use to calibrate the various capital regimes without needing to make adjustments to the underlying accounting?

With the significant diversity of products, economies, legal and business environments across the globe, it is unrealistic to expect that adjustments, eliminations and scalars can fully align disparate regimes. Such adjustments, eliminations and scalars can be useful to provide as much comparability as is possible but they should not be overworked to the detriment of a cost effective final result.

State Farm Mutual continues to believe that reliance on the concepts developed and implemented for the insurance industry by its primary regulators can be appropriately applied in these circumstances to insurance companies significantly engaged in insurance activities and regulated by the Board as SLHCs.

The ACLI's proposed A&C approach includes scalars that attempt to calibrate capital requirements based on the relationship of normal operating capital levels to the required capital levels in each regime. This relationship can be used to scale up or down other regimes to the baseline regime. Where the scalar attempts to equalize differences resulting from differences in underlying accounting rules (i.e. conservatism in reserve levels) it may be appropriate to adjust both required capital and available capital. For other scalars that attempt to equalize regulatory stringency, only required capital should be adjusted. Past history of insolvencies and pre-event capital levels may provide insight into the effectiveness of the regimes' capital requirements including regulatory trigger points in detecting companies approaching capital inadequacy.

As indicated in the answer to question 7, the Board may wish to consider the development and application of a safe harbor applicable to domestic insurers with non-U.S. insurer affiliates to minimize the burden of scaling foreign regimes or re-stating financials into a compatible regime for scaling. Consideration should be given to adopting the option to use a 50% risk charge on the available capital of such subsidiaries or affiliates. This is consistent with the charge for such affiliates in the U.S. RBC formula.

Question 18. How should the BBA address inter-company transactions?

Intercompany transactions that, when aggregated, inappropriately impact required capital or available capital should be adjusted for. The economic substance of the transactions should drive the need for adjustments.

Question 19. What criteria should be used to develop scalars for jurisdictions? What benefits or challenges are created through the use of scalars?

As noted in the response to questions 16 and 17, the use of scalars can help normalize different accounting frameworks especially where it impacts capital requirements. However as previously stated, one must consider that the capital requirements in the various jurisdictions are based on the accounting standards also in use in those jurisdictions. Thus, both the required capital and available capital are developed using the same accounting framework.

The ACLI's proposed A&C approach includes scalars that attempt to calibrate capital requirements based on the relationship of normal operating capital levels to the required capital levels in each regime. This relationship can be used to scale up or down other regimes to the baseline regime. Where the scalar attempts to equalize differences resulting from differences in underlying accounting rules (i.e. conservatism in reserve levels) it may be appropriate to adjust both required capital and available capital. For other scalars that attempt to equalize regulatory stringency, only required capital should be adjusted. Past history of insolvencies and pre-event capital levels may provide insight into the effectiveness of the regimes' capital requirements including regulatory trigger points in detecting companies approaching capital inadequacy.

Question 20. What are the costs and benefits of a uniform, consolidated definition of qualifying capital in the BBA?

Use of the definitions of qualifying capital under the existing regimes would be appropriate. Leveraging existing regulatory frameworks and supervisory tools should be a key attribute in the Board's approach for insurance centric SLHCs. There is little benefit to the added layers of complexity brought on by new/multiple definitions of qualifying capital.

Question 21. If the Board were to adopt a version of the BBA that employs a uniform, consolidated definition of qualifying capital, what criteria should the Board consider? What elements should be treated as qualifying capital under the BBA?

As long as a financial capital instrument is subordinate, either contractually or structurally to policyholder obligations, it should be recognized as an available capital resource. It should be noted that for mutual organizations the use of subordinated surplus notes, subject to strict regulatory control, act much like traditional capital and should be treated similarly in alignment with treatment under U.S. RBC.

Question 22. Should the Board categorize qualifying capital into multiple tiers, such as the approach used in the Board's Regulation Q? If so, what factors should the Board consider in determining tiers of qualifying capital for supervised institutions significantly engaged in insurance activities under the BBA?

As noted in the response to question 20, use of the definitions of qualifying capital under the existing regimes would be appropriate. Leveraging existing regulatory frameworks and supervisory tools should be a key attribute in the Board's approach for insurance centric SLHCs. There is little benefit to the added layers of complexity brought on by new/multiple definitions of qualifying capital.

Consolidated Approach Questions 23 – 37:

State Farm Mutual believes the BBA is a workable framework for all Board regulated companies significantly engaged in insurance activities. The Consolidated Approach ("CA") contemplated by the ANPR has the potential for dangerously advancing the notion that capital is freely fungible within an insurance group, thereby undermining the longstanding legal-entity framework of insurance that serves as the very foundation of any effective rule tailored to the insurance business model. The BBA with its aggregation of existing solvency measures for the underlying entities within a holding company provides an effective balance between the goals of policyholder protection and financial stability of the broader capital markets.

Question 23. What are the advantages and disadvantages of applying the CA to the businesses and risks of supervised institutions significantly engaged in insurance activities?

In weighing the strengths and weaknesses of the CA as identified by the Board, it is difficult to balance seemingly conflicting goals. The existing regulatory capital frameworks for insurance operations provide an effective measure of risk and the required capital to support it. Therefore, depending upon the granularity and sophistication of the CA insurance risk segments and factors, the CA may not adequately measure the needed capital for such operations.

However, with more complex organizations, with multiple and varied business segments, the CA's use of consolidated information (assuming it is available in the necessary format) may provide more streamlined groupings and risk measurements for the multiple business segments. The CA appears to be a much less tailored approach which then magnifies the need for its benefits, expected to be derived from a less complex and more standardized approach, to outweigh the cost of a less risk sensitive measure. It is difficult to judge this balance without significantly more detail as to the risk segments and factors under consideration.

It is believed that where the regulated entity is predominately engaged in insurance activities regardless of size, the BBA produces a good result. Thus the risk profile of the regulated entity may be a key determinate of the best approach to apply.

State Farm Mutual is concerned that the CA has the potential for dangerously advancing the notion that capital is freely fungible within an insurance group, thereby undermining the longstanding legal-entity framework of insurance that serves as the very foundation of any effective rule tailored to the insurance business model.

Question 24. What are the likely challenges and benefits to the development, implementation, and application of the CA? To what extent could the CA efficiently use existing records, data requirements, and systems, and to what extent would the CA require additional records, data, or systems?

As the Board recognizes, should the CA ever be applied to a non-GAAP U.S. regulated entity, the costs and challenges would be overly burdensome. State Farm Mutual strongly believes the costs would in fact outweigh the benefits given the viable alternatives and based on an understanding of the significant upfront and ongoing effort that would be needed to design the appropriate systems, control frameworks and processes to support this additional and separate "consolidated" reporting.

Question 25. To what extent would the CA be prone to regulatory arbitrage?

The ANPR does not provide a definition of regulatory arbitrage and without detailed information about the risk segments and regulatory adjustments used in the CA, it is difficult to fully respond to this question. However, U.S. insurers are subject to uniform state-based holding company statutes and regulations that subject all material inter-affiliate transactions to prior regulatory review and disapproval. This has and will prevent or minimize potential arbitrage as it relates to regulated insurance entities within a holding company system as the current regulatory framework is consistent and equitable across U.S. domestic regulatory jurisdictions.

Question 26. Is the CA an appropriate framework to be applied to systemically important insurance companies? What are the key challenges to applying the CA to systemically important insurance companies? How effective would the CA be at achieving the goals of ensuring the safety and soundness of a systemically important insurance company as well as minimizing the risk of a systemically important insurance company's failure or financial distress on financial stability?

As noted in the response to question 23, in weighing the strengths and weaknesses of the CA as identified by the Board, it is difficult to balance seemingly conflicting goals. The existing regulatory capital frameworks for insurance operations provide an effective measure of risk and the required capital to support it. Therefore, depending upon the granularity and sophistication of the CA insurance risk segments and factors, the CA may not adequately measure the needed capital for such operations.

However, with more complex organizations, with multiple and varied business segments, the CA's use of consolidated information (assuming it is available in the necessary format) may provide more streamlined groupings and risk measurements for the multiple business segments. The CA appears to be a much less tailored approach which then magnifies the need for its benefits, expected to be derived from a less complex and more standardized approach, to outweigh the cost of a less risk sensitive measure. It is difficult to judge this balance without significantly more detail as to the risk segments and factors under consideration.

It is believed that where the regulated entity is predominately engaged in insurance activities regardless of size, the BBA produces a good result. Thus the risk profile of the regulated entity may be a key determinate of the best approach to apply.

Question 28. What should the Board consider in developing a definition of qualifying capital under the CA? What elements should be treated as qualifying capital under the CA?

As noted in the response to question 21, as long as a financial capital instrument is subordinate, either contractually or structurally to policyholder obligations, it should be recognized as an available capital resource. It should be noted that for mutual organizations the use of subordinated surplus notes, subject to strict regulatory control, act much like traditional capital and should be treated similarly in alignment with treatment under U.S. RBC.

Question 30. What risk segmentation should be used in the CA? What criteria should the Board consider in determining the risk segments? What criteria should the Board consider in determining how granular or risk sensitive the segmentation should be?

As with the BBA approach, the Board should leverage to the greatest extent possible the existing insurance RBC frameworks for the business segments of the regulated entity. Where organizational complexity or the materiality of non-regulated business segments make the BBA type approach overly complex or burdensome then the CA's more simplified aspects could be considered.

Question 32. What are the pros and cons of using the risk segmentation framework in the proposed Consolidated Financial Statements for Insurance Systemically Important Financial Institutions as the basis of risk segmentation for the CA?

The property and casualty risk segments which appear to closely match existing U.S. SAP definitions would be beneficial to use. The life risk segments, however, do not match existing U.S. SAP definitions and would prove more difficult to use. To the extent international business is combined into common segments, the diversity of product characteristics and the underlying economic and legal environments for such products may significantly undermine the intended benefits of such risk measurement standardization.

Question 33. How should the CA reflect off-balance-sheet exposures?

To the extent off-balance sheet exposures are already identified in existing regimes, as with U.S. RBC, they should be used.

Question 35. What considerations should the Board apply in determining the various factors to be applied to the amounts in the risk segments in the CA?

Consistent measures of risk severity or confidence levels should be pursued (e.g. 1 in 70).

Question 36. What challenges are there in determining risk factors for global risks?

The lack of homogeneity of products offerings and underlying economic, legal and business climate across the jurisdictions is a major challenge for standardization of risk classification and measurement.

Question 37. What criteria should the Board consider in developing the minimum capital ratio under the CA and a definition of a "well-capitalized" or "adequately capitalized" insurance institution?

Regulatory action triggers of existing regulatory solvency frameworks should be considered. The CA, like the BBA, should leverage to the extent possible the existing capital frameworks applied to the regulated entities.

Other Approaches:

Question 38. Should the Board reevaluate any of these approaches? What additional consideration, if any, should the Board give to any of the regulatory capital approaches discussed above?

While State Farm Mutual supports the BBA as an appropriate framework, State Farm Mutual also encourages the Board to reevaluate and move towards its identified alternative that relies exclusively on state insurance solvency requirements for SLHCs that have a regulated insurance company as the top-tier parent of the group. State Farm Mutual has highlighted Congress's directions to the Board to avoid supplanting state regulation of insurance for federally supervised insurance companies to the greatest extent practical. These directions apply to all facets of insurance company operations - from capital to accounting. These directions are consistent with Congress's authorization of the Board to accept state insurance regulation as sufficient to satisfy any federal "consolidated" regulatory requirements where the SLHC itself is a regulated insurance company. Therefore, since the BBA recognizes the validity and adequacy of existing functional multi-faceted regulation to which the SLHC or its affiliates and/or subsidiaries are already subject, State Farm Mutual believes it is wholly within the Board's discretion to simply defer to the existing insurance RBC framework and capital requirements for such top-tier insurance SLHCs and insurance SLHCs generally.

Consistent with Congressional intent, where the SLHC itself is a regulated insurance company, there is no need for the Board to re-invent the wheel. Deference to the existing state-based RBC framework and capital requirements for such companies should be the standard unless the Board makes a specific determination that such state requirements are inadequate for federal supervisory purposes. In the case of State Farm Mutual, this would imply utilization solely of State Farm Mutual's insurance RBC, without the need for further, additional capital measurement.

Other Comments:

Stress-Testing:

Closely tied to capital adequacy is risk assessment and stress testing. Of particular note, there is significant opportunity for the Board to leverage the ORSA requirements in lieu of establishing a separate stand-alone stress testing requirement, should the Board ever contemplate such a need for SLHCs. As noted above, State Farm Mutual's ORSA provides a comprehensive review of its enterprise risk management framework, risk identification, measurement and management processes, economic capital modeling, stress testing, and capital adequacy assessment. State Farm Mutual's ORSA is prepared on a group basis that includes the impact of intercompany risk transfer, diversification or other intra-group transfers which should alleviate the Board's concerns with aggregating legal entity stress tests. State Farm Mutual's ORSA can be effectively utilized for federal supervisory purposes, as needed. Importantly, any approach the Board utilizes to monitor capital and solvency of an SLHC should continue to recognize the legal entities within the group and the explicit restrictions, which the Board itself has previously recognized, on the transferability of funds between legal entities within a group. For regulated insurance groups, capital is not freely transferrable across different entities within the group and any group capital measurement should explicitly recognize this reality.