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

RE: Docket No. R–1539; RIN 7100 AE 53 Capital Requirements for Supervised Institutions Significantly Engaged in Insurance Activities

Dear Federal Reserve Board of Governors:

The National Association of Mutual Insurance Companies ("NAMIC") appreciates the opportunity to comment on the Federal Reserve Board ("FRB") Advanced Notice of Proposed Rulemaking ("ANPR") entitled "Capital Requirements for Supervised Institutions Significantly Engaged in Insurance Activities." This ANPR represents an important first step toward devising a cost effective and applicable group capital requirement for insurers that own depository institutions.

NAMIC is the largest property/casualty insurance trade association in the country, with more than 1,400 member companies representing 39 percent of the total market. NAMIC supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers. NAMIC member companies serve more than 170 million policyholders and write more than $230 billion in annual premiums. Our members account for 54 percent of homeowners, 43 percent of automobile insurance, and 32 percent of the business insurance markets. Through our advocacy programs we promote public policy solutions that benefit NAMIC member companies and the policyholders they serve and foster greater understanding and recognition of the unique alignment of interests between management and policyholders of mutual companies.

NAMIC supports the general direction the FRB has proposed in the ANPR regarding capital requirements for insurers under its supervision. The incorporation of the Insurance Capital Standards Clarification Act of 2014 with the FRB's own requirements for holding company capital requirements illustrates insight into the differences between insurers and banks. NAMIC members are pleased with the use of National Association of Insurance Commissioners' ("NAIC") Statutory Risk-Based Capital ("RBC") requirements and with the rejection of a market consistent valuation approach. NAMIC also agrees with the justification for rejecting the approaches to insurance group capital utilized in the European Union's Solvency II and the International Association of Insurance Supervisors' ("IAIS") draft

Insurance Capital Standard ("ICS"). The expression of FRB views on these alternatives will no doubt change the debate internationally.

NAMIC is also pleased that the FRB approached this effort with an ANPR that proposes a structural concept, but also includes several open questions about the details. This approach is preferred in rulemaking as the details of the actual formula, the capital required, and capital resources available will require input from insurers with varying corporate structures. As is always true in complex financial rulemaking, the details are critical. We are appreciative that our U.S. regulators provide interested parties with the opportunity to provide such comments as our regulators work through the process. This collaborative approach is one of the hallmarks of our system that should be advanced internationally. We salute the FRB for taking the lead on a national level by providing transparency in rulemaking.

NAMIC intends for its comments on behalf of our membership to be constructive in assisting the FRB in developing future, more detailed iterations of this ANPR. We propose some revisions and clarifications as well as suggestions for additional details to advance the rulemaking process. We are always willing to answer questions and discuss concerns with representatives from the FRB if a dialogue would be useful.

I. INTRODUCTION -- COMMENTS AND QUESTION RESPONSES

NAMIC supports the general direction the FRB has proposed in the ANPR regarding capital requirements for insurers under their supervision. The incorporation of the Insurance Capital Standards Clarification Act with the FRB's own requirements for holding company capital requirements illustrates the FRB insight into the differences between insurers and banks. NAMIC members, who generally are not required to file financial reports on a GAAP basis, are also pleased with the use of NAIC Statutory Accounting Principles and RBC requirements. Finally, the FRB decision to pursue a capital structure based on aggregating state insurance regulatory capital requirements is consistent with the limitations of federal law. Consistently applying these concepts to the Building Blocks Approach ("BBA") framework will provide a meaningful way to measure insurance group capital.

The laws bringing savings and loan holding companies ("SLHCs") under the FRB supervision are relatively recent in their implementation, especially as such laws apply to insurance SLHCs ("ISLHC"). Following the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("DFA") —which transferred the regulatory authority for SLHCs from the Office of Thrift Supervision to the FRB -- several FRB regulatory promulgations have specifically exempted ISLHCs until specific capital and supervisory requirements could be designed. The enactment of the Insurance Capital Standards Clarification Act in 2014 provided the FRB with clear legal authority to address the differences between ISLHCs and other depository institution holding companies. Before finalizing the capital standard, the FRB will want to make revisions to ensure compliance with various supervisory standards and laws that apply to insurance depository institution holding companies ("IDIHC") engaged in insurance activities.

The ANPR is a good first step in designing a system for insurance group capital. As the FRB continues to develop the details of its group capital standard, NAMIC would like to highlight the following considerations:

- NAMIC believes that the BBA would be suitable for all insurance groups; however, any decision to subject an insurance group to a Consolidated Approach must be based solely on a determination by the Financial Stability Oversight Council that the insurer could pose a threat to the financial stability of the U.S.
- As the FRB moves toward adding more details to the proposal they should make note of federal laws that impose limitations on the FRB's ability to impose capital requirements on insurance subsidiaries of IDIHCs and limitations on the requirement that IDIHCs serve as a source of strength to their depository institution subsidiaries.
- Also in regulating ISLHCs it is important to note that they are all currently subject to limitations on permissible activities of the grandfathered thrifts they own pursuant to the Qualified Thrift Lender Test.
- Finally, NAMIC recommends removing from any subsequent proposal language referring to entities not supervised by the FRB or presumptions about how other insurance groups might be regulated in order to avoid prejudicing any future policy decision-making on insurance group capital standards.

A. Supervisory Standards

For insured depository institution ("IDI") entities the FRB is expected to develop regulations that will ensure the safety and soundness of the IDI (12 USCS §1831p-1); and for IDIHCs the FRB is expected to develop regulations that ensure the holding company acts as a source of strength for the IDI (12 USC §1831). In the case of insurance entities there are limitations on these supervisory standards (12 USC §1831o-1;12 USC §1844(g)). The FRB rulemaking may not exceed the authority provided by law, and any attempts to regulate the insurance entities within the holding company would be actions beyond FRB authority.

"*12 USC* §1844 Administration

. . . .

(g) Authority of State insurance regulator and the Securities and Exchange Commission.
(1) In general. Notwithstanding any other provision of law, any regulation, order, or other action of the Board that requires a bank holding company to provide funds or other assets to a subsidiary depository institution shall not be effective nor enforceable with respect to an entity described in subparagraph (A) if—
(A) such funds or assets are to be provided by—
(i) a bank holding company that is an insurance company, . . .; or
(ii) an affiliate of the depository institution that is an insurance company. . . ; and
(B) the State insurance authority for the insurance company . . . determines in writing sent to the holding company and the Board that the holding company shall not provide such funds or assets because such action would have a material [materially] adverse effect on the financial condition of the insurance company . . ."

Section 1844(g) exists to prevent the FRB from requiring movement of an insurance entity's assets or funds to the IDI resulting in material adverse impact on the financial condition of the insurer. While this is significant, additional federal laws ensure that the FRB cannot even require such provision of assets to satisfy the "source of strength" standard. 12 USC §1831o-1.

> "12 USC §1831o-1. Source of strength
> . . . .
> (c) Authority of state insurance regulator.
> (1) In general. The provisions of section 5(g) of the Bank Holding Company Act of 1956 ([12 U.S.C. 1844(g)]) shall apply to a savings and loan holding company that is an insurance company, an affiliate of an insured depository institution that is an insurance company, and to any other company that is an insurance company and that directly or indirectly controls an insured depository institution, to the same extent as the provisions of that section apply to a bank holding company that is an insurance company.
> (2) Rule of construction. Requiring a bank holding company that is an insurance company, a savings and loan holding company that is an insurance company, an affiliate of an insured depository institution that is an insurance company, or any other company that is an insurance company and that directly or indirectly controls an insured depository institution to serve as a source of financial strength under this section shall be deemed an action of the Board that requires a bank holding company to provide funds or other assets to a subsidiary depository institution for purposes of section 5(g) of the Bank Holding Company Act of 1956 ([12 U.S.C. 1844(g)])." (Emphasis added)

In short, the U.S. Code provides that the FRB defer to state insurance regulators before imposing an additional capital requirement on any insurance subsidiary of an IDIHC over and above the state insurance regulatory requirement. In addition, the FRB cannot require an IDIHC to serve as a "source of strength" if the state insurance regulator says that such action would have a "materially adverse effect" on the financial condition of an insurance entity. These laws and limitations are similarly applied to FDIC actions pursuant to 12 USC §1831v.

The laws illustrate clear congressional intent for the FRB to defer to state insurance regulators for solvency and capital oversight. This intent should be honored regardless of whether the FRB believes the state RBC standard is sufficient. The BBA in the ANPR adheres to this principle by aggregating the insurance legal entity RBC requirements, but implications in the ANPR of revisions, additions or changes to the state RBC requirements are not supported by federal law as long as those entities are in compliance with state insurance requirements.

A further illustration of congressional intent was recently included in the Insurance Capital Standards Clarification Act of 2014 (12 USCS § 5371(c)) wherein the FRB is even authorized to eliminate all insurance entities in an IDIHC from their requirements for leverage and risk-based capital for depository institution holding companies.

> *"12 USC §5371*
> (c) Clarification.
> (1) In general. In establishing the minimum leverage capital requirements and minimum risk-based capital requirements on a consolidated basis for a depository institution holding company or a nonbank financial company supervised by the Board of Governors as required under paragraphs (1) and (2) of subsection (b), the appropriate Federal

> banking agencies shall not be required to include, for any purpose of this section (including in any determination of consolidation), a person regulated by a State insurance regulator or a regulated foreign subsidiary or a regulated foreign affiliate of such person engaged in the business of insurance, to the extent that such person acts in its capacity as a regulated insurance entity. (Emphasis added)

While the FRB has not proposed the approach of eliminating the insurance entities from its capital calculations, the law does not require them to do so. However, the FRB is bound to abide by the limitations on capital requirements set forth in federal law (12 USC §1831o-1; 12 USC §1844(g)). Leaving the insurance entities to the state insurance regulators for application of RBC requirements and adding those requirements to Basel III requirements for the IDIs and the non-insurance affiliates seems the best approach. For all of these reasons NAMIC:

- Recommends limiting the BBA group capital requirements to aggregation of state RBC for insurance legal entities at Company Action Level (200 percent ACL) for BBA companies;
- Recommends that the only supervisory standard for any insurance entity within a depository institution holding company should be "policyholder protection" to avoid overstepping the bounds of federal law and the authority of the state insurance regulators.
- Recommends very minimal eliminations and adjustments from state RBC requirements and state admitted capital – only addressing elimination of duplicative requirements; and
- Recommends the inclusion of surplus notes and senior debt in the capital resources included as available capital for consistency with the policyholder protection goal and compliance with federal laws.

B. Financial Stability

Financial stability is critical to our economy and to all business and individual interests in the United States. Identifying preventable behavior that has caused instability in the past and may cause it in the future should be a primary role of financial institution regulators. Further, under the DFA the Financial Stability Oversight Counsel ("FSOC") is charged with reducing financial instability by designating organizations as Systemically Important Financial Institutions ("SIFIs"). Finally, promulgating enhanced prudential standards for SIFIs and closely monitoring them for preventable behaviors that can cause systemic risk is critical for success in achieving consistent financial stability. Protecting financial stability is an important goal for the FRB in regulating the SIFIs but the ANPR suggests that financial stability and maintaining companies on a "going concern" basis should be the standard for the BBA capital requirements as well. This distinction between the two supervised groups should be clarified in the next draft of the proposed rule.

In the U.S., insurance regulation has been designed to protect policyholders; it is not intended to avoid all possibilities of insurance company failure. In other words, it is neither designed to protect insurers as "going concerns" nor to protect bondholders and creditors from loss. If insurance subsidiaries are to be regulated—whether by an insurance regulator or by the

FRB—Congress has made it clear that they are to be regulated pursuant to state insurance regulatory goals and not impacted with higher levels of capital by the FRB as discussed above.

In addition, requiring companies to hold capital at high enough levels to reduce the losses that caused the 2008 financial crisis would cause those companies to have a significant competitive disadvantage. Moreover, higher capital requirements also result in higher prices for customers. In the end, relying on group capital to ensure financial stability will not be successful, will result in higher premiums and reductions in the supply of insurance, serving neither the goal of financial stability nor the goal of policyholder protection.

Fortunately, capital is not the only tool that can be used by supervisors to address solvency risks. State regulators can identify potential systemic risks and address specific products or activities of individual companies or insurance groups with much more targeted tools than increased capital requirements. For example:

- Broad based tools like the NAIC Model Insurance System Holding Company Act ("HCA") can help with identification of such risks. The HCA provides for the financial examination of all affiliates, access to books and records of all affiliates, enterprise risk reporting on the significant risks at the ultimate parent level, and group supervision for the entire enterprise. The HCA provides a system of "windows and walls" that allow insurance regulators to examine and investigate beyond the insurance affiliates to identify enterprise risk, while also protecting the insurer's surplus for the benefit of policyholders.
- The Risk Management Own Risk and Solvency Assessment Model Act ("ORSA") provides for annual comprehensive internal assessments of Enterprise Risk Management ("ERM") including the company's (or group's) framework for ERM, risk tolerances and appetites, assessment of risk exposures, group risk capital assessment and development, stress testing, and prospective solvency assessment. This is required of all insurance companies with $500 million or more in premium and insurance groups with $1 billion or more in premium.
- Should regulators identify specific activities of specific companies that are increasing the potential for systemic risk, they can act to address those activities using targeted tools. Such tools can include concentration limits, investment restrictions to address liquidity or risky ventures, ERM risk limits or requirements, required restructuring of an insurance organization, receivership/insolvency and elimination of authority to write new policies.

NAMIC agrees that financial stability is important and that entities that have been designated as SIFIs should be subject to enhanced prudential regulation to address this issue. The continuation of these companies as "going concerns" has been deemed important to our economy. The same cannot be said of the ISLHCs. None of them have been designated as SIFIs and, therefore, none of them are considered too-big-to-fail. Even if their importance as SLHCs further magnifies their impact on the economy or changes the supervisory standard from "policyholder protection" to "source of strength" for the depository institutions they own, there are many other regulatory devices that can be used by the FRB to satisfy this concern. Tools like investigations, reporting/disclosures, leverage requirements, ERM, group supervision/oversight, liquidity requirements, injunctions, and cease and desist orders, will give the FRB the information about risks and the authority to take necessary action. The limitations on what the FRB can require in terms of capital or assets from insurance entities under federal law reveal the weaknesses of using capital to manage the risks. For all of these reasons, NAMIC:

- Recommends that a capital standard designed to achieve national "financial stability" should not be applied to any entity that has not been designated as a systemically important financial institution (SIFI);
- Recommends that regulatory tools other than capital available to state regulators or the FRB be used to address any perceived heightened risks for ISLHCs.

II. RESPONSES TO SPECIFIC QUESTIONS – TWO OPTIONS

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? We agree that all of the identified considerations are appropriate. We suggest the addition of a consideration regarding the federal laws limiting the application of added capital requirements or added assets or funds for insurance entities as outlined in the discussion above of Supervisory Standards section I.A. We also suggest an additional consideration related to leveraging insurance solvency practices and procedures. This could include information gathering through engagement with supervisory colleges and the use of ORSA stress testing to satisfy similar goals of the FRB.

Question 2. Should the same capital framework apply to all supervised insurance institutions? We understand the FRB's need to provide a different level of calibration for SIFIs even if the same capital framework is applied. Please note, however, that if a mutual company were designated as a SIFI the FRB should provide flexibility for such a company to proceed under the BBA for consistency with the Insurance Capital Standards Clarification Act.

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? NAMIC agrees with the proposal in the ANPR. A supervised insurance institution should be subject to regulatory capital rules tailored to the business of insurance if one or more of the group's entities is regulated by a state insurance supervisor, licensed as an insurance company and is either a top-tier savings and loan holding company that is an insurance underwriting company, or has 25 percent of total assets (excluding insurance underwriting of credit risk) in insurance underwriting 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? If the appropriate measurement of the holding company's risk is used to develop capital needs, then the capital framework will be successful. We understand the FRB's need to provide a different level of calibration for SIFIs even if the same capital framework is applied. Non-designated ISLHCs should be subject to an aggregation-type capital requirement subject to the limitations of federal law.

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?
The only other parameters in addition to insurance underwriting activities that will be useful in determining if an institution is significantly engaged in insurance activities would be assurances that one or more of their affiliate or subsidiary entities are licensed as an insurance company and regulated by a state insurance regulator.

III. GENERAL COMMENTS: BUILDING BLOCK APPROACH

NAMIC supports the general direction the FRB has proposed in the ANPR regarding capital requirements for insurers under their supervision. The incorporation of the Insurance Capital Standards Clarification Act with the FRB's own requirements for holding company capital requirements illustrates the FRB insight into the differences between insurers and banks. NAMIC members, who generally don't file financial reports on a GAAP basis, are also pleased with the use of NAIC Statutory Accounting and RBC requirements. Finally, the FRB decision to pursue a capital structure based on aggregating state insurance regulatory capital requirements is consistent with the limitations of federal law previously outlined. Consistently applying these concepts to the BBA framework will provide a meaningful way to measure insurance group capital. Despite the strength of this ANPR there are some opportunities for improvement and issues that should be addressed.

A. Scalar

The draft provides little information about how or when the FRB intends to apply calibration or use scalars. NAMIC suggests that it is important not to over-complicate the issue as there will not be a perfect solution. In the best of circumstances, capital requirements are estimated amounts that provide some protection to the policyholders or depositors of the supervised institutions. They never completely solve the problems of poor management or illegal behavior. Only regulatory oversight, reporting and investigation/examination can uncover such problems. For this reason, NAMIC favors a simple scalar that results in an accounting agnostic comparison between different jurisdictions and sectors. Scalars can be used to calibrate regulatory stringency in required capital between regimes or to calibrate both regulatory stringency and fundamental differences in the underlying accounting frameworks which may make the relationships between normal operating capital levels and required capital levels different between regimes.

B. Legal, Contractual and Structural Subordinated Debt

The FRB ANPR includes several references to "double leveraging" in the discussion about contractual and structural subordinated debt (surplus notes and senior debt) as a form of qualifying capital. These forms of debt were discussed as potential intercompany eliminations. Contractual and structural subordinated debt is used to protect policyholders and is accepted as qualifying capital (a.k.a. "admitted assets") by the state insurance regulators. The elimination of these forms of qualifying capital for insurance entities especially when issued to third parties, may well violate 12 USC §1844(c)(3)(A) and Reg. Q which protect bank holding companies and SLHCs from changes in requirements that are in compliance with the capital requirements of the state insurance regulator. The elimination of the surplus note or senior debt proceeds serving as qualifying capital of an insurance entity would be a direct violation of this law. NAMIC suggests that to avoid this issue the FRB should follow the aggregation approach and consider both contractual and structural subordinated debt as capital at the legal entity level instead of eliminating this capital completely from the analysis.

The subordinated status of this debt to the interests of policyholders is also important in this analysis. The interest payments on surplus notes are legally subordinated to the interests of policyholders and can only be made with the approval of the state insurance regulator. In this manner, surplus notes support the goal of policyholder protection and should be aggregated under the BBA framework. The interest payments on senior debt are obligations of the holding company, not the insurance affiliate and will only be paid if there are holding company assets to pay them. In the event of insolvency these amounts are not owed by the insurance affiliate so they are considered structurally subordinate to policyholders. Since the value of surplus notes and senior debt cannot drastically decline or increase, they are less volatile instruments than common stock as well.

C. International Companies

We are concerned about language in the ANPR suggesting the BBA may not work satisfactorily for insurance groups with international companies. While most of the companies that would be subject to the BBA have limited involvement internationally, negative statements about the BBA and international companies can unnecessarily influence the discussions in other fora. NAMIC urges the FRB to eliminate this language as it begins to raise questions about further regulatory segmentation of the industry that are outside the scope of the rulemaking.

D. Stress Testing
There are references in the ANPR to stress testing for ISLHCs. At the state regulatory level, the NAIC ORSA requires annual comprehensive internal assessments of Enterprise Risk Management ("ERM") including the company's (or group's) framework for ERM, risk tolerances and appetites, assessment of risk exposures, group risk capital assessment and development, stress testing, and prospective solvency assessment. This is required of all insurance companies with $500 million or more in premium and insurance groups with $1 billion or more in premium. While there may be differences between the stress testing envisioned by the ORSA and stress testing for SLHCs and BHCs under Reg YY, the ORSA stress testing is designed for insurance companies and can be an efficient source of information. Additional stress testing requirements for ISLHCs should be unnecessary.

III. RESPONSES TO SPECIFIC QUESTIONS – BBA FRAMEWORK

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? As long as the BBA framework remains simple and the FRB does not exceed state insurance regulatory requirements (see NAMIC Comment Letter section IA), we see only advantages to using this approach. The use of existing RBC requirements for insurers provides a strong basis used by prudential insurance regulators and a cost-effective approach to the development of an appropriate capital requirement for IDIHCs that engage in insurance activities. A new, complex capital regime for twelve ISLHCs and two SIFIs is unnecessary and would be unreasonably costly for all. Once the final framework is decided upon a capital requirement based on the aggregation of RBC for the insurance legal entities could be implemented with little delay. The only simpler approach would be to eliminate the insurance entities from the group capital analysis altogether, as the FRB is authorized to do under the Insurance Capital Standards Clarification Act.

The ANPR suggests several perceived weaknesses to this BBA framework. We disagree that the aggregation of legal entity capital is a weakness as this is the only approach in the current environment that will provide accurate information honed to the risk profiles of each legal entity that is capable of quick implementation and reasonable accuracy. Despite all best efforts no capital requirement is perfect.

We do not agree with the FRB's discussion of potential regulatory arbitrage under this BBA approach. In fact, the similarity to state RBC requirements will result in reduced potential for such arbitrage, since states provide consistent reporting and regulatory supervision across all insurance entities through the HCA, consistent ORSA assessments and stress testing, and consistent principles for the state RBC requirements providing policyholder protection. NAIC HCA requires reporting, enterprise risk management and regulatory supervision of all holding companies including an insurer's non-insurance affiliates. The state supervisors must either approve or not disapprove all material intercompany transactions making it a regulatory violation for groups to move capital to other jurisdictions without the regulator's knowledge. For all of these reasons the FRB would have the full support of the state insurance regulators in enforcing the rules and assuring there is no gaming of the system.

The disadvantage identified in the ANPR regarding extensive intercompany adjustments will be reduced as the FRB learns more about the existing information available, the regulatory reporting, and the corporate structure of each of the twelve regulated groups it oversees. The suggested weakness of calculating scalars could be minimized by eliminating the unnecessary scalars between U.S. states with permitted practices. Such practices are usually limited to a single company and are temporary as they are created to deal with a specific transition. The only scalar identified related to prescribed practices is for New York. Finally, the concern about legal-entity-level stress testing can be alleviated by using the ORSA stress testing for the BBA holding companies instead of trying to design unique testing.

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? To answer this fully we need to see more details about the BBA approach. The challenges with the BBA proposal will all depend on how complicated the FRB decides to make the capital requirement. We suggest a few key themes:

- Simple aggregation with very limited adjustments and eliminations and no scalars between states relying on state regulatory judgement. This is consistent with federal law as well as state law.
- For non-insurance affiliates, the FRB is advised to utilize materiality thresholds and to leave non-insurance affiliates that support insurance operations in under the RBC calculations.
- It is imperative that reporting be on an annual basis and not a quarterly basis.
- NAIC Statutory Annual Statements, RBC reports, and any GAAP reporting for non-insurance affiliates will provide all of the details needed. Since SAP reporting is a form of GAAP and much of the non-insurance reporting is done on a GAAP basis no reconciliation between SAP and GAAP is recommended.

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?

There are at least three levels of potential scalars to be considered.

- International Jurisdictions to the U.S.
- Insurance to Banking or other non-insurance sectors
- Property-Casualty to Life

While the first two categories are self-explanatory, in addition to accounting for differences between solvency regimes, scalars also need to account for material differences between sectors within a regime such as in the U.S. between the property-casualty and life industries as companies with similar financial strength operate at different RBC ratios. In short, while the local intervention level (company action level) for US-Life insurers and P&C insurers is the same, there are distinctions in how life and P&C insurers manage to these capital requirements and in how they are assessed by regulators.

NAMIC believes that significant work will be required to confirm the efficacy of any scalar developed, so we would advise a simple scalar formula at the outset.

Changes in the scalars will also need to be managed carefully allowing adequate time for companies to grow into a changing requirement. We suggest that the changes be made infrequently – no more than annually – and with sufficient time for companies to comply,

Question 9. To what extent is the BBA prone to regulatory arbitrage? The BBA framework's similarity to state RBC requirements will result in reduced potential for such arbitrage since states provide consistent reporting and regulatory supervision across all insurance entities through the HCA, consistent ORSA assessments and stress testing, and consistent principles for the state RBC requirements providing policyholder protection. NAIC HCA requires intercompany transaction reporting, enterprise risk reports and regulatory supervision of all holding companies including an insurer's non-insurance affiliates. The state supervisors must either approve or not disapprove all material intercompany transactions making it a regulatory violation for groups to move capital to other jurisdictions without the regulator's knowledge. For all of these reasons the FRB may rely upon state insurance regulators in enforcing the rules and assuring there is no gaming of the system.

Additionally, the capital requirements the FRB imposes on IDIs should protect the banking entity from regulatory arbitrage and the individual insurance legal entities have RBC requirements under state insurance law to protect their policyholders from similar concerns. Federal Reserve supervisory powers and state insurance regulatory powers under the Insurance Holding Company Act enacted in all states will provide both state and federal regulators with the opportunity to oversee any capital movements taking place that might be related to differences in the state and federal regulatory systems.

Question 10. Which jurisdictions or capital regimes would pose the greatest challenges to inclusion in the BBA? Regimes that do not use valuation systems consistent with U.S.

GAAP/SAP will create challenges. Regimes that have advanced solvency systems that differ from the U.S. legal entity RBC approach may also be problematic (Solvency II, C-ROSS, Japanese approach). However, if an accounting agnostic scalar is used it will produce the simplest means to compare systems. In general, jurisdictions that receive an observing or largely observing score on their Insurance Core Principle ("ICP") 17 assessment by the IMF could be considered comparable to the U.S. simplifying the scalar calculation.

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? The ISLHCs with an RBC-reporting insurer as the ultimate parent company create no additional challenges compared to companies with an ultimate parent that is not an insurance RBC reporting entity. In fact, this organizational structure will include an RBC charge for all of the affiliates and subsidiaries that are part of the group, whether insurance or non-insurance in operations. All segments of these groups would be completely subject to the holding company act, expected to be incorporated in ORSA summary reports and all accounted for in the R0/C0 element of the RBC for the top tier company.

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?
Yes. The key strengths of the BBA include the following: (i) it efficiently uses existing legal-entity-level regulatory capital frameworks; (ii) it is an approach that could be developed and implemented expeditiously; (iii) it would involve relatively low regulatory costs and burdens for the institutions; and (iv) it would produce regulatory capital requirements that are tailored to the risks of each distinct jurisdiction and line of business of the institution. The IDIHC's safety and soundness is addressed by the dual regulatory system. With both state insurance regulatory and FRB supervisory oversight of the holding company there is a better chance that issues arising within the holding company will be identified and the consistency of the capital requirement will assure that both regulators are understanding the changes in the holding company and addressing concerns. Incremental safety and soundness benefits are also complemented by the lower additional compliance costs due to the smaller number of scalars involved.

Question 13. Would the BBA be appropriate for larger or more complex insurance companies that might in the future acquire a depository institution?
The concern expressed in the ANPR that the BBA may not be appropriate for "larger or more complex insurance depository institution holding companies" and that such larger and or more complex companies might be subject to a regulatory capital framework other than the BBA is misplaced. Even if a firm is systemically important, the BBA will effectively assess the firm's

group capital, regardless of the size, complexity, or international business of such an organization. There is no need for the FRB to contemplate a different regime than the BBA for such insurance groups.

Question 14. In applying the BBA, what baseline capital requirement should the Board use for insurance entities, banking entities, and unregulated entities? For U.S. insurance entities, we agree that the state insurance regulatory RBC is the appropriate baseline capital requirement. For foreign insurance entities, we believe the baseline requirement should be the domicile jurisdictional capital requirement. And for banking entities we agree that the proper baseline is Basel III. For unregulated entities the R0/C0 and R2/C1 factors for insurance and non-insurance affiliates under state RBC requirements provide a reasonable means to assess capital requirements for the insurance entities. In the case of ISLHCs with an insurer as the top tier parent, the current RBC captures all aspects of their group. This is the direction the NAIC is leading, and it has significant promise for a sound group capital calculation.

Question 15. How should the BBA account for international- or state-regulator-approved variances to accounting rules? For international accounting differences the use of a scalar can provide a reasonable means of comparison. For state regulator permitted or prescribed practices for an individual company, the reliance should be on the state regulator to make the correct decision considering all of the circumstances that company faces.

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? Scalars will address true regulatory and operating differences. The only adjustments we think make sense are adjustments when companies have used off-shore companies to avoid statutory accounting requirements. These amounts should be restated on a statutory basis. The changes to the capital aggregation should be as limited as possible. By consistently following the aggregation concept we can avoid overcomplicating the issue.

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? We agree with the use of accounting agnostic scalars that compare the actual average operating capital held by companies in a jurisdiction to the average regulatory required capital levels to compare what is actually taking place in jurisdictions. This will not require adjustments to accounting. Adjustments may be needed to avoid the elimination of surplus notes and senior debt from the qualifying capital altogether. This addition would not be a double leveraging situation, but instead one in which the FRB recognizes the capital transferred from the parent to the insurance affiliate as capital available to resolve policyholder obligations.

Question 18. How should the BBA address intercompany transactions? To answer this question, more information is needed about the transactions under consideration. The only intercompany transactions NAMIC thinks make sense to address are those related to off-shore companies set up to avoid statutory accounting requirements. As stated in the answer to Question 16, these amounts should be restated on a statutory basis.

Question 19. What criteria should be used to develop scalars for jurisdictions? What benefits or challenges are created through the use of scalars? Scalars make the most sense if they are accounting agnostic, and if they look at the actual functioning of insurers in the jurisdiction instead of the regulatory requirements alone. There are too many potential differences between reserving requirements, litigation environment, government backing, other insurance solvency oversight, regulatory tools available, and other means of protecting policyholder interests like guaranty funds, to allow for a common approach. That is the reason for the use of an objective scalar like the actual average operating capital held by companies in a jurisdiction to the average regulatory required capital levels to compare what is actually taking place in jurisdictions. This will provide a much better measure to compare the capitalization of entities in varying jurisdictions.

Question 20. What are the costs and benefits of a uniform, consolidated definition of qualifying capital in the BBA? If we are going to accept capital requirements across multiple jurisdictions we need to accept those jurisdictions' definitions of qualifying capital as well. Undoing that definition will result in changing the whole concept of the aggregation approach. We encourage the FRB to be true to the aggregation approach and accept the capital that is allowed by the jurisdictional insurance regulator. If disclosures can help identify areas of concern from company to company, we would not be opposed to that approach.

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? We do not agree with a uniform, consolidated definition of qualifying capital under the BBA. But if such a definition were to be developed under the aggregated BBA, we would support one that provided a look-through to the legal entity prudential regulatory admitted capital and not a listing of different instruments that are qualifying and non-qualifying.

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?

No, multiple tiers are not needed with this approach. Under the aggregation approach and the look-through to prudential insurance regulators for their capital requirements and qualifying capital, capital is capital. Tiering only further complicates the calculation with limited value.

NAMIC will continue to work with the Federal Reserve and other stakeholders, and will advocate for productive legislative and regulatory developments for our members. If you have questions or comments, also please feel free to contact me at 317-876-4270, mrogers@namic.org.

RESPECTFULLY SUBMITTED,

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