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September 16, 2016

Robert deV. Frierson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551
E-mail: regs.comments@federalreserve.gov

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

Dear Mr. Frierson,

Thank you for the opportunity to share our views on the Federal Reserve Board's (Board) Advanced Notice of Proposed Rulemaking (ANPR) covering capital framework proposals for systemically important financial institutions (SIFIs) and insured depository institution holding companies (IDIHCs) under the Board's regulatory authority.

Dodd-Frank Title I establishes the authority for the Board to regulate non-bank SIFIs, however, these institutions, together with IDIHCs, have been subject to solvency regulation on a state basis for over 100 years. Over that time, state regulators developed and continuously enhanced a comprehensive set of tools, practices, and protocols that represent the financial regulatory framework and processes for insurers. The existing state-based financial regulatory framework is comprised of required approvals and restrictions that limit insurers' activities (e.g., licensing requirements, change in control, dividends, affiliate transactions, reinsurance, etc.), required financial reporting in accordance with conservative statutory accounting principles and the monitoring of financial results to identify situations where prompt corrective action is warranted to avoid failures, and lastly, a financial back stop (i.e., guaranty funds) that provide policyholder protection in the event of an insolvency.

Historically, the continuously enhanced suite of state-based regulatory tools, practices and protocols have proven enormously effective in monitoring and managing insurer capital adequacy. Accordingly, while recognizing the expanded regulatory authority of the Board pursuant to Dodd-Frank, it is our strong recommendation that the Board preserve and enhance, and not replace, the existing state-based, highly customized and effective regulatory capital framework, the national consistency of which is managed by the National Association of Insurance Commissioners (NAIC) through its rigorous state accreditation program.

Moreover, despite the different primary regulatory goals of the Board (i.e., stability of the financial system) and state insurance commissioners (i.e., protection of policyholders) we that believe the Board and the NAIC (acting as the representative of state commissioners) can capitalize on this unique opportunity to formally establish their respective entities as "governance partners" and work to synergistically combine their objectives in an attempt to fully leverage the existing highly effective regulatory capital framework and enhance it to address in a more direct manner the regulatory objectives of the Board.

Instead of fully leveraging and enhancing the existing NAIC administered insurance regulatory framework as its starting point, the Board proposed two separate and new capital measurement frameworks; one for SIFIs and another for IDIHCs. The IDIHC proposal is described as a Building Block Approach (BBA) where available and required capital measures are obtained from existing regulatory frameworks (e.g., NAIC Risk-Based

Capital - "NAIC RBC", Solvency II, etc.) and modified through the application of scalars and other adjustments. In contrast, the Board's proposed Consolidated Approach (CA) for SIFIs represents an entirely new risk-based capital measurement framework requiring the use of U.S. GAAP-based financial information where available.

The ANPR focuses largely on the measurement of assets, liabilities, and residual capital of regulated insurance groups even though that is only one element of an effective financial regulatory oversight framework. More specifically, a financial regulatory oversight framework should address required approvals and restrictions that limit insurers' activities, required financial reporting including its form, content and periodicity, monitoring of financial results to identify situations where prompt corrective action is warranted to avoid failures, and a financial back stop to provide policyholder protection or to protect the financial system from systemic risk in the event of an insolvency.

In evaluating the two proposed measurement frameworks we note that they do not address the following key components of a comprehensive financial regulatory oversight framework.

- A specified target level of capital for the BBA and CA considered adequate for insurance groups operating under the oversight authority of the Board
- Specific powers, authority, and the expected range of actions expected to be available to the Board in instances where insurance groups or underlying insurance subsidiaries of a regulated insurance group fail to maintain predetermined target levels of required capital
- Expectations of how the Board might interact with domestic and international insurance regulators in situations where insurance groups (as well as components of insurance groups) under its authority fail to maintain predetermined target levels of required capital
- In addition, on a broader oversight basis, the Board also has not identified what it sees as the principal risks facing the insurance industry and how it may address those risks through capital requirements for those entities under its regulatory authority.

Beyond the missing elements of a comprehensive financial regulatory oversight framework, we have specific concerns with the BBA and CA proposals. For example, the proposal to permit modifications of NAIC RBC outputs through application of scalars and other proposed (e.g., consolidation) adjustments should be well defined and very limited. More specifically, we believe that if the Board observes the need for significant modifications to NAIC RBC measurement outputs, a dialogue between the Board and NAIC should occur to determine if NAIC RBC measures should be modified in lieu of the Board requiring the modification of outputs or developing an entirely new capital framework. In the case of scalars we believe their use should be limited to adjustments for <u>intra</u>-framework differences (e.g., Permitted Practices that cause inconsistencies in the computation of required or available capital) and <u>inter</u>-framework differences (e.g., different capital adequacy target levels inherent in different frameworks applied - e.g., NAIC RBC and Solvency II - that otherwise would produce inconsistent levels of required or available capital).

We strongly advocate for a single framework that fully utilizes the time-tested, historically effective NAIC RBC framework and other capital frameworks (e.g., Solvency II) determined to be sufficiently robust in their construction to permit the use of their "outcomes" on a largely unadjusted basis, excluding the intra- and inter-framework differences referenced above, when computing the capital adequacy of an insurance group. Moreover, in assessing group capital adequacy, we consider the identified capital framework as not simply an assessment of mathematical metrics, but rather a comprehensive, integrated program that combines capital adequacy benchmarks with a highly interactive oversight process involving regulators, regulated insurers, and regulatory tools such as the Own Risk and Solvency Assessment, supervisory colleges, and other continuous interactions between the insurer and regulators where regulators obtain a broad and deep understanding of the risks and opportunities faced by the insurer.

On site examinations, including state regulator completed financial statement and operational audits are critical in that they allow insurance regulators to assess the current solvency of insurers and develop a prospective view of an insurer's exposure to risk and its risk management practices. The effectiveness of the on-site examination emerges from the regulator's direct interaction with management and its ability to observe and evaluate corporate governance processes and practices, the function and effectiveness of the board of directors and management, the adequacy of enterprise risk management practices, and the identification and discussion of all significant risks facing the insurer, both currently and prospectively. It is through this type of dialogue that the regulator can proactively obtain information about emerging risks such as those related to the long-term care product, the Affordable Care Act exchanges, asbestos and environmental exposures, all of which have now materialized but before emerging could have been identified together with the insurer's plan to monitor, mitigate, and manage the risk where necessary and to evaluate its impact on current and longer-term capital adequacy through the consideration of the risks in stress testing performed by the insurer. Moreover, the NAIC authors very comprehensive and specific statutory reporting requirements that anticipate the availability and use of financial data and risk measures in computing RBC.

The CA, as currently proposed by the Board, requires the use of U.S. GAAP information where available which is not entirely consistent with requirements and objectives of the Insurance Capital Standards Clarification Act of 2014 (Act). The Act provides that a regulated insurer shall not be required to develop U.S. GAAP financial statements in situations where they are not already prepared and available. The ANPR suggests that because complex, international, systemically important firms typically prepare financial statements under U.S. GAAP, requiring their use where available to apply the CA proposal would be less burdensome. In our view, the availability and use of statutory and U.S. GAAP based financial information is critical in terms of measuring capital adequacy and disclosing the results of the evaluation to the insurers principal stakeholders (e.g., policyholders, shareholders, creditors, etc. - depending on whether the insurer is a mutual or stock company). In the case of mutual companies owned by policyholders, consistent with our support of the NAIC RBC framework, the exclusive use of statutory-based financial information would be appropriate as it would be used to complete the NAIC RBC evaluation which is consistent with the basis of the financial information used in the financial statements prepared for owners/policyholders. In contrast, for stock companies that will also apply the NAIC RBC framework, they must reconcile their statutory-based equity to their U.S. GAAP-based equity to disclose to shareholders and creditors of the U.S. GAAP-based parent of the insurer the capital adequacy of the insurance components of the entity. At the same time, the capital adequacy of any non-insurance elements of the GAAP-based reporting entity with external shareholders and creditors must be evaluated considering the outcomes of capital adequacy frameworks applied to those non-insurance activities (e.g., Basel III applied to banks, etc.).

Assessing the capital adequacy of individual components of the parent company (which can be either a mutual insurance company or a U.S. GAAP-based holding company) is critical as it permits, in the case of insurers, the completion of stress testing of the separately regulated entities that hold capital. Moreover, the critical importance of the Board and state-based regulators working directly with the insurer is that it allows the identification and evaluation of risks facing the insurer currently and in the future. It is vital that these risks be discussed collaboratively between the Board, relevant state insurance regulators, and the insurer to allow appropriate stress testing and evaluation of capital adequacy. The results of the stress testing are discussed and evaluated by the principal parties on a strictly confidential basis and the proposed capital plans (including dividends - including those to shareholders and policyholders - share buy backs, acquisitions, etc.) of the regulated entity are evaluated and either approved or modified.

Another reason the Board and state-based regulators must work together is to reconcile and prioritize the regulatory objectives. While the broad regulatory objectives of the Board and state-based regulators are consistent, the relative or prioritization of those objectives differ. More specifically, the primary objective of the Board is the safety and soundness of the insured depository institution and its effect on the financial stability of the financial system followed closely by policyholder protection. In contrast, the primary objective of state-based insurance supervisors is the protection of policyholders. As a result of the Board's "top down", or financial system stability focus, versus state-based regulator's "bottom-up", or policyholder focus, requires the parties to work together on a proactive basis to understand the risks and opportunities facing the regulated entity and to develop coordinated, proactive plans to address risks and opportunities through the ongoing evaluation, approval, and/or modification of the capital plans of the regulated entity. Addressing risks and opportunities on a proactive basis allows the parties to identify alternatives that appropriately balance the interests of stakeholders before such time that a risk emerges and creates a crisis situation with limited available actions, including those that are not balanced with respect to their impact on individual groups of stakeholders. Accordingly, we urge the Board to work closely with state regulators to develop a framework that fully utilizes the state-based framework and to modify it, as necessary to meet the objectives of the Board and allow the Board and state insurance regulators to work together as effective governance partners. In addition, by working together as effective governance partners, the Board and state regulators can proactively address regulatory decisions that produce unintended outcomes.

We are concerned that the CA does not specifically acknowledge the lack of capital fungibility between separately regulated insurance subsidiaries of an insurance group. In reality, insurers typically hold the majority of their capital in the underlying operating insurance entities and move capital to the holding or parent company subject to regulatory guidelines and approvals for distribution to shareholders or other re-deployment. In our view, performing capital adequacy evaluations on a consolidated basis implies a level of capital fungibility that does not exist. Our concern is that a consolidated view of capital adequacy may produce an inaccurate view of capital sufficiency where excess capital in one separately regulated insurance legal entity within a group is not available to cover deficiencies at other subsidiary entities (insurance or otherwise). Accordingly, aggregating outcomes of each legal entity's capital assessment remains the best way to assess an insurance group's capital adequacy.

We also note that the Board suggests the CA could be quickly developed and implemented due to the initial goal to achieve broad risk segmentation and the belief that a focus on the consolidated insurance group provides a more appropriate basis for conducting stress tests. In contrast, we observe that there is substantial work necessary to develop a set of appropriately calibrated risk factors and weights for major segments of assets and insurance liabilities even if initially constructed with a lower level of precision. In addition, a separate statutory-based version of the CA is necessary if the CA were to be applied to an insurer that only prepares financials using statutory accounting principles. Moreover, due to the aforementioned lack of capital fungibility, we believe stress testing on a legal entity basis remains a more compelling objective than consolidated testing so we do not see consolidated testing as an inherent benefit of the CA model.

In summary, we strongly encourage the Board to adopt a single capital framework for all insurance entities under its regulatory authority consistent with the Board's BBA proposal. We believe this represents the optimal solution and would allow the Board and NAIC (acting as representative of state commissioners) to capitalize on the unique opportunity to formally establish their respective entities as "governance partners," work to synergistically combine their objectives in an attempt to fully leverage the existing highly effective regulatory capital framework, and enhance it to address in a more direct manner the regulatory objectives of the Board. In our view, achieving a high level of harmonization between the Board's group capital proposals and NAIC RBC would lead to more consistent, efficient, and effective regulatory outcomes.

Thank you for considering our comments and we hope you find our observations helpful.

Sincerely,

Sam Pilch	Kevin Spataro
Senior Group Vice-President and Controller	Senior Vice President, Corporate Accounting Research
Allstate Insurance Company	Allstate Insurance Company

APPENDIX

Responses to ANPR Questions

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 believe the comprehensive list of considerations are appropriate. In addition, we believe a high level of coordination between the Board and state insurance regulators is vital, both in the development of a regulatory capital framework and also in its application. We believe the interests of policyholders, shareholders, and creditors where applicable, are best served when the Board and state insurance regulators operate as "governance partners". Moreover, proactive engagement between the Board, state insurance regulators and insurers is vital to ensure that actions are thoroughly evaluated from the perspective of all stakeholders, balanced, and give appropriate consideration to the potential for unintended consequences.***

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

> ***Yes. A single capital framework (i.e., the BBA) should be applied to all supervised insurance institutions. We support the sole application of the BBA as it most substantially leverages the existing historically effective state-based regulatory capital framework. Moreover, recognizing the need for the Board and state regulators to operate as governance partners, it is vital that the capital framework be a shared product.***

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?

> ***We support the Board's proposed threshold of at least 25% of total consolidated assets in insurance underwriting subsidiaries (other than assets associated with insurance underwriting for credit risk). Similarly, we support the Board's proposal to define "systemically important insurance companies" that would apply the designated capital framework to non-bank financial companies identified by the Financial Stability Oversight Council with at least 40% of total consolidated assets related to insurance activities (as of the end of either of the two most recently completed fiscal years).***

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?

> ***We support the application of a single group capital framework to all supervised insurance institutions. The single group capital framework applied should be the one that represents the framework required in the geographical area where the principal insurance activities take place and where the principal insurance operating companies are domiciled.***

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?

> ***No response.***

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?

The advantage of the BBA is that it leverages existing, effective, customized jurisdictional capital frameworks (e.g., NAIC RBC for US insurers, Basel III for banks, etc.).

- ***The NAIC RBC framework was designed and has been continuously enhanced by state insurance regulators over many years. The NAIC RBC framework has a long history of effectiveness and provides the Board and state insurance regulators with an appropriate tool to support their work as effective governance partners.***
- ***The BBA determines group capital adequacy based on an aggregation of capital resources and capital requirements across legal entities within an insurance group. We believe the building block framework supports sound regulatory assessments as it assumes capital does not move freely between subsidiaries without prior regulatory approval or meeting pre-established regulatory guidelines.***

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?

Because the BBA leverages existing capital frameworks, the infrastructure and process (i.e., records, data requirements, systems, etc.) used to administer the capital frameworks should be readily available. Moreover, given the leveraging of the NAIC RBC framework in the BBA model, it allows the Board the opportunity to interact with state regulators to enhance an already effective framework as opposed to the alternative task of constructing an entirely new framework.

The principal challenge of the BBA is in limiting the application of scalars and adjustments to preserve the consistency of the outputs.

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?

The use of scalars should be limited to necessary adjustments for intra-framework differences (e.g., permitted practices that would otherwise allow inconsistencies in the computation of required capital) and inter-framework differences (e.g., different capital adequacy target levels inherent in different frameworks - e.g., NAIC RBC versus Solvency II that otherwise would produce inconsistent levels of required capital).

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

We do not see a material risk of regulatory arbitrage in the BBA. More specifically, we believe the inherent transparency of the BBA reduces the likelihood of regulatory arbitrage as capital levels will be available at a more granular level (compared to the CA) which allows stakeholders to observe the amount of capital attributable to BBA components and how those amounts change over time which is more likely to reveal situations where regulatory arbitrage is being used (compared to the CA). In addition, assuming a substantial leveraging of all material elements of the existing insurance regulatory capital framework, we believe the ancillary oversight requirements and activities such as completion of the Own Risk and Solvency Assessment, participation in supervisory colleges, and other regular interactions with

management where regulators obtain an understanding of the risks and opportunities faced by the insurer may also reveal any regulatory arbitrage actions.

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

The greatest challenges are presented by non-U.S. subsidiaries (insurance or non-insurance) related to geographies that involve unique risks that are not easily identifiable and measurable and which present a substantial calibration challenge.

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?

In the case of a supervised insurer owning another supervised insurer, the principal stakeholders of both supervised insurers that require regulatory capital adequacy information include policyholders, shareholders of the parent supervised insurer and creditors, if any. The BBA would aggregate available and required capital of the supervised insurers (parent and subsidiary) along with any non-insurance entities. U.S. statutory-based financial information would be used to complete the NAIC RBC evaluations for both the parent and subsidiary supervised insurers and the capital attributable to the parent's investment in any non-insurance subsidiaries would be completed with a Basel-like approach (i.e., an appropriate capital charge would be applied to the parent's investment in the non-insurance business). There should be no requirement in this case to perform a Statutory to U.S. GAAP reconciliation, provided the interests of the principal stakeholders are supported by an insurance operation that is required to prepare both its financial statements and regulatory capital computations using U.S.-statutory accounting principles.

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 BBA is an appropriate framework to apply to insurance depository institution holding companies as it leverages the underlying capital adequacy frameworks applicable to the insurance and banking businesses. In contrast, performing a capital adequacy evaluation on a consolidated basis could produce a false positive outcome if it assumes excess capital is freely movable out of an insurance company which is not the case.

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

Yes, for the reasons noted above, in the event a supervised insurance parent were to acquire a supervised bank it would be appropriate to apply the BBA to the group. More specifically, pursuant to the BBA, the customized regulatory capital frameworks for banks and insurance companies would be applied to the components of the group and evaluated on a combined basis. Recognizing the same constraint that excess capital is not freely movable outside of predetermined limitations, it is entirely appropriate to perform the capital adequacy evaluation on an aggregated versus consolidated basis, as a consolidated evaluation could produce a false positive outcome if it assumes excess capital is freely movable out of an insurance company, which is not the case.

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

The baseline capital requirement for insurance entities and banking entities should be consistent with requirements set forth in the capital frameworks applied to the entities by their principal regulator that produce a level of regulatory capital necessary to allow the entities to operate without regulatory intervention. For example, for insurance companies subject to NAIC RBC, we believe the "Company Action Level" of regulatory capital should be targeted as a floor against which regulatory capital sufficiency would be evaluated.

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

We believe this is one of the limited instances where "Scalars" could be used to adjust for intra-framework differences (e.g., permitted practices) that would otherwise create inconsistencies in the computation of required capital.

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 principal challenge when aggregating different accounting and capital adequacy frameworks is in appropriately reconciling the target level of desired regulatory capital between the frameworks. The strength of the BBA, assuming the underlying accounting framework (e.g., IFRS) and capital framework (e.g., Solvency II) are sufficiently robust, is that the accounting information used to populate the capital adequacy framework was specifically designed for that information.

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?

Scalars could be used to address inter-framework differences (e.g., NAIC RBC, Solvency II, Swiss Solvency, etc.)

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

Material inter-company transactions should be disclosed, including their impact on reported and regulatory capital. Disclosure allows stakeholders to evaluate the nature of the transaction and to make adjustments to capital adequacy measures if that is deemed appropriate. Moreover, it is relevant to note that insurance regulators are required to approve most material inter-company transactions.

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

The principal objective when developing scalars is in reconciling to a desired common level of regulatory capital between regimes. The principal benefit of scalars is that, assuming the capital regimes are sufficiently robust, accounting information developed under different frameworks can be used in the capital adequacy tool specifically designed for that information. The principal challenge for scalars is the same as the principal objective. More specifically, reconciling different capital adequacy frameworks to a common level of regulatory capital is a significant challenge. While the exercise cannot achieve a very high level of precision given the inherent complexities of the different frameworks, we still believe the exercise can generate sufficiently reliable outputs to support the value of the process.

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

> ***We believe a uniform definition of qualifying capital is necessary as it relates to each framework aggregated in the BBA. Moreover, the definition should describe the capital in terms of its principal attributes. Without a consistent definition of qualifying capital the BBA cannot be relied upon to produce consistent and useful outputs.***

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?

> ***The objective of an insurance group capital requirement should be primarily policyholder protection with creditor and shareholder protection as a secondary objective. In determining capital adequacy, we believe it important to consider all forms of capital that are structurally subordinate to policyholder obligations. In addition to traditional capital (i.e., common equity), insurers regularly access capital through issuance of surplus notes, senior debt, appropriately structured subordinated debt, preferred stock, and other instruments. Moreover, it is worth noting that insurers' access to additional forms of capital allowed them to successfully weather the 2008 financial crisis. If only common equity had qualified as capital, insurers and their shareholders would have been very adversely impacted as the cost of capital and resulting dilution from issuing common equity in the 2008 financial crisis would have been very significant.***

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?

> ***If the Board adopts the BBA we believe it would be useful for qualifying capital to be categorized into tiers representing the quality of the capital determined by its ability to absorb losses during economic stress.***

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?

> ***We do not see any advantages to the CA. Disadvantages of applying the CA are as follows:***
>
> - ***The CA does not leverage the existing time tested U.S. insurance regulatory framework. It would require insurance groups to implement an entirely new untested capital framework.***
> - ***The CA, as currently drafted, requires the use of U.S. GAAP information where available which is not entirely consistent with the requirements and objectives of the Insurance Capital Standards Clarification Act of 2014, and does not consider the fact that for many insurance groups with a U.S. GAAP reporting parent, separate U.S. GAAP financial statements for individual operating subsidiaries are often not available. Therefore, if this were to be a requirement it would likely be enormously costly both monetarily and in terms of personnel time.***
> - ***The CA adopts a consolidated view of capital which implies a level of capital fungibility that does not exist. The ANPR states that part of its objective is "ensuring that holding companies can serve as a source of strength for any subsidiary insured depository institution." The CA does not consider that insurers typically hold the majority of their capital in operating insurance subsidiaries and move excess capital to the holding or***

parent company subject to specific regulatory guidelines and approvals for distribution to shareholders or other re-deployment. A consolidated view of capital adequacy may produce an inaccurate view of capital sufficiency, where excess capital in one separately regulated insurance legal entity within a group is not available to cover deficiencies at other subsidiary entities (insurance or otherwise).

- *The ANPR suggests that a focus on the consolidated insurance group provides a more attractive basis for conducting stress tests, however, due to the lack of capital fungibility between individual entities within the group, we believe the most relevant stress testing analysis is developed on an individually regulated entity basis.*
- *The ANPR suggests the CA can be quickly developed and implemented due to initial broad risk segmentation. In our view it would be an enormous task, one that would take many years to complete, to develop a set of appropriately calibrated risk factors and weights for major segments of assets and insurance liabilities. Moreover, if constructed, a separate statutory-based version would also be necessary to conform with the requirements of the Act.*

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 an entirely new, untested framework, development of the CA would require significant time and resources to develop and implement, not just on the part of the Board but also for SIFIs and other insurance entities that the Board may, in the future, deem sufficiently large and complex to warrant application of the CA. The new CA framework would require the evaluation of many diverse insurance risks related to underwriting, claims, mortality, investment risk, liquidity, credit exposure, etc. for purposes of developing risk factors to be applied to exposures when determining the level of required capital. The new metrics may require new records, systems, and data requirements which would need to be maintained.

Because it is an entirely new framework, development and implementation of the CA would be a lengthy process - likely a time period between 5 to 10 years - and would be enormously expensive; monetarily and in terms of personnel and other resources. In contrast, the BBA could be implemented in a relatively short time-frame, and because it leverages output from existing sources and systems, it would be relatively inexpensive to implement both monetarily and in terms of personnel and other resources.

If the CA were to be applied to an insurance group that only develops statutory-based financial statements, which are not prepared on a consolidated basis, the development and implementation period would be further extended.

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

We consider the risk of regulatory arbitrage to be relatively low for both the BBA and the CA. More specifically, all comprehensive regulatory systems (which would include the envisioned BBA and CA) involve much more than mathematical computations. That is, the frameworks are supported by on-site examinations that involve direct interaction with management which allows an evaluation of corporate governance processes, practices and material transactions, the function and effectiveness of the board of directors and management, the adequacy of enterprise risk management practices, and the identification and discussion of all significant risks facing the insurer, both currently and prospectively. These evaluations would likely reveal material regulatory arbitrage actions if they exist.

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?

> ***We believe the BBA is the most appropriate framework to be applied to insurers under the regulatory authority of the Board, including SIFIs. The BBA measures risks and capital adequacy based on the existing capital frameworks that have been determined to be sufficiently robust in their construction to permit the use of their "outcomes" on a largely unadjusted basis (excluding adjustments for intra- and inter-framework differences for permitted practices and differences in capital adequacy target levels between the frameworks applied). Further, the BBA specifically address the risks of the particular entity (e.g., insurance versus banking) and measurements and adequacy assessments can be performed at the operating entity level where business is conducted. Because the BBA utilizes capital measures developed at the operating entity level, it addresses the fact that capital is not freely moveable between individually supervised entities and thus a capital shortfall in one entity within a group cannot be supplemented by excess capital in a separately regulated entity.***

Question 27. What should the Board consider in determining more stringent capital requirements to address systemic risk? Should these requirements be reflected through qualifying capital, required capital, or both?

> ***We believe systemic risk should be addressed by required capital. More specifically, instruments and practices that cause systemic risk must first be identified and once identified, should be assessed an appropriate capital charge to create an economic disincentive to reduce or eliminate the systemically risky activity. We believe the Board has significant experience in implementing similar measures in the U.S. banking system and the general design of those disincentives should be transferrable to insurance groups.***

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?

> ***Qualifying capital should be consistently defined for purposes of the BBA and CA. In developing the definition of qualifying capital, the Board should consider whether the capital is available to the entity to absorb losses during economic stress. This would include all forms of additional capital that are structurally subordinate to policyholder obligations. In addition to traditional equity insurers regularly access capital through issuance of surplus notes, senior debt, preferred stock, subordinated debt and other instruments.***

Question 29. For purposes of the CA, should the Board categorize qualifying capital into multiple tiers? What criteria should the Board consider in determining tiers of qualifying capital for supervised institutions significantly engaged in insurance activities under the CA?

> ***Yes, for purposes of developing the CA and developing the definition of qualifying capital, the Board should consider to what extent the capital is available to absorb losses under economic stress. The more losses that can be absorbed for a longer period of time, the higher the tier (or quality) of capital.***

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?

We do not support further development of the CA.

Question 31. What challenges does U.S. GAAP present as a basis for segmentation in the CA?

The principal challenge is that the CA is an entirely new framework and given the significant differences between it and NAIC RBC, it will be challenging to initially reconcile the outcomes of the CA and BBA utilizing NAIC RBC.

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?

We do not support further development of the CA.

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

We do not support further development of the CA.

Question 34. Under what circumstances should U.S. GAAP be used or adjusted to determine the exposure amount of insurance liabilities under the CA?

We do not support further development of the CA.

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?

We do not support further development of the CA.

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

We believe the challenges are relatively straight forward. More specifically, all material risks should be evaluated in relation to an insurers' capital determined either on a legal entity, group, regional, national, or international basis. Risk factors should be determined and applied based on the risks they pose at each level of consideration and their level of systemic exposure. For example, if the global reinsurance market were concentrated in a relatively small number of very large global reinsurers then the failure of any one of those reinsurers could cause a high level of exposure to systemic risk. To address and curtail the risk, capital charges would be specifically determined in a manner to both protect the existing ceding companies and to dis-incent any further elevation of the existing level of systemic risk.

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

We would support the use of "adequately capitalized" principally because we believe the level should be above a regulatory action level which is the case with "adequately capitalized". Moreover, once the regulatory action level is exceeded we see no benefit in setting the minimum capital ratio at "well capitalized" versus "adequately capitalized".

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?

> ***We do not believe the Board should reevaluate any of the other approaches considered (i.e., bank focused capital framework, only assessing capital requirements for non-insurance entities, a capital framework based on Solvency II, and a capital framework based on stress testing).***