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Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Submitted via Email

Re: <u>Regulatory Capital Rules: Risk-Based Capital Requirements for Depository Institution Holding Companies Significantly Engaged in Insurance Activities, Docket No. R—1673, RIN 7100—AF 56</u>

Dear Ms. Misback:

Teachers Insurance and Annuity Association of America ("TIAA") appreciates the opportunity to comment on the Board of Governors of the Federal Reserve System's (the "Board") notice of proposed rulemaking on risk-based capital requirements for depository institution holding companies significantly engaged in insurance activities (the "NPR").[1] The formulation of capital requirements that are tailored to reflect insurance companies' unique business model is of critical importance for insurance-centric savings-and-loan holding companies ("ISLHCs") like TIAA, and we are grateful for the Board's thoughtful approach to the issue.

We are strongly supportive of the Board's proposed "building block approach" ("BBA") used to calculate an enterprise-wide capital requirement. Additionally, we are appreciative of the Board's efforts to align the requirements set forth in the NPR with existing requirements under state insurance regulatory regimes. We believe the NPR, once finalized, will provide ISLHCs with an appropriate insurance-based capital regime. However, we believe the NPR could be strengthened and improved by certain modifications and clarifications, as discussed further below. We respectfully submit these recommendations for the Board's consideration.

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[1] *Regulatory Capital Rules: Risk-Based Capital Requirements for Depository Institution Holding Companies Significantly Engaged in Insurance Activities*, 84 Fed. Reg 57240 (Oct. 24, 2019), *available at*: https://www.govinfo.gov/content/pkg/FR-2019-10-24/pdf/2019-21978.pdf.

I. About TIAA.

Founded in 1918, TIAA is the leading provider of retirement and financial services for those in academic, research, medical, and cultural fields. Over our century-long history, TIAA's mission has always been to aid and strengthen the institutions and participants we serve and to provide financial products that meet their needs. To carry out this mission, we have evolved to include a range of financial services, including asset management and retail services. Today, TIAA manages over $1 trillion in assets, and our investment model and long-term approach aim to benefit the five million retirement plan participants we serve across more than 15,000 institutions.[2] With our strong nonprofit heritage, we remain committed to the mission we embarked on in 1918 of serving the financial needs of those who serve the greater good.

TIAA was originally incorporated as a stock life insurance company in the State of New York, and is a licensed insurer in all 50 states, the District of Columbia, and Puerto Rico. TIAA is a privately held, wholly owned subsidiary of the TIAA Board of Overseers ("Overseers"), a special purpose New York not-for-profit corporation. Over the last century, the TIAA enterprise has grown to offer a diverse array of financial services, including asset management and retail banking. Among TIAA's subsidiaries is TIAA, FSB, a federal savings bank with total assets of approximately $40 billion. By virtue of their ownership of TIAA, FSB, TIAA and Overseers are registered as savings-and-loan holding companies ("SLHCs") and are subject to supervision and regulation by the Board under the Home Owners' Loan Act ("HOLA").

II. TIAA strongly supports the Board's proposed BBA framework.

TIAA appreciates the time, attention, and effort the Board has devoted to designing capital requirements that are appropriately tailored for ISLHCs. We especially applaud the Board's adoption of the BBA, which "constructs 'building blocks' – or groupings of entities in the supervised firm – that are covered under the same capital framework [and] are then used to calculate the combined, enterprise-level available capital and capital requirement."[3] We were strongly supportive of the BBA proposed in the Board's 2016 advance notice of proposed rulemaking on this same topic (the "ANPR"),[4] as reflected in the comment letter submitted by the Insurance Coalition, a group of federally supervised insurance companies that includes TIAA (the "2016 Comment").[5] We agree with the 2016 Comment that the BBA is a desirable approach, as it "can be appropriately applied to any institution regardless of size, ownership type. . . corporate structure, breadth of business, countries of operation or any other distinguishing attributes." The BBA also "avoids disruption of the state insurance regulatory regime" and "addresses all material non-insurance subsidiaries through reliance

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2 Data are as of September 30, 2019.

3 84 Fed. Reg. at 57244.

4 *Capital Requirements for Supervised Institutions Significantly Engaged in Insurance Activities*, 81 Fed. Reg. 38631 (June 14, 2016), *available at*: https://www.govinfo.gov/content/pkg/FR-2016-06-14/pdf/2016-14004.pdf.

5 *See* Letter from the Insurance Coalition to the Board re: ANPR (Sep. 16, 2016), *available at*: https://www.federalreserve.gov/SECRS/2017/May/20170526/R-1539/R-1539_091616_130522_456951221165_1.pdf.

on existing capital regimes. . .” Likewise, we believe that the BBA described in the NPR, which is substantively similar to the version proposed in the 2016 ANPR, is well calibrated to reflect the unique business models and needs of ISLHCs.

III. TIAA requests clarification on the application of capital calculations under Section 171 of the Dodd-Frank Act.

Section 171 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Section 171”) requires in part that the Board establish minimum capital requirements for depository institution holding companies.[6] These requirements may not be less than the “generally applicable” capital requirements for insured depository institutions (“IDIs”), nor quantitatively lower than the capital requirements that applied to IDIs on July 21, 2010.[7] Amendments made to Section 171 in 2014 permit the Board to exclude companies engaged in the business of insurance from these capital calculations (the “2014 Amendments”).[8]

In an effort to comply with Section 171, the Board is proposing to require ISLHCs to conduct Section 171 capital calculations (“Section 171 Calculations”) using “the flexibility afforded under the 2014 amendments to [Section 171] to exclude certain state and foreign regulated insurance operations and to exempt top-tier insurance underwriting companies.”[9] This requirement would apply separately from and in addition to the Board’s proposed BBA framework for ISLHCs. In the case of a top-tier ISLHC that is not an insurance underwriting company, the top-tier holding company would be required to apply the Section 171 Calculations. Where the top-tier holding company is itself an insurance underwriting company, the Section 171 Calculations would apply to the farthest upstream savings-and-loan holding company in the organization that is not an insurance underwriting company. The entity that conducts the Section 171 Calculations may choose not to consolidate the assets and liabilities of its subsidiary insurance companies for purposes of these calculations, consistent with the 2014 Amendments. In that case, the NPR proposes that the entity either (a) deduct the amount of the entity’s outstanding equity interest in its subsidiary insurers, or (b) apply a 400 percent risk weight to its outstanding investment in its subsidiary insurers.[10]

A. ISLHCs should not be required to conduct separate Section 171 Calculations if they satisfy the requirements of the proposed BBA framework.

As an initial matter, TIAA believes that an ISLHC’s compliance with the BBA framework proposed in the NPR should be sufficient to satisfy the requirements of Section 171, such that the ISLHC should not be required to conduct separate Section 171 Calculations. We note that Section 171 does not directly require ISLHCs to conduct two separate capital calculations; rather, Section 171 mandates that the Board establish minimum capital requirements for ISLHCs, according to certain standards set forth in that section. In order to

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6 Pub. L. No. 111-203, Title I §171, 124 Stat. 1376, 1435 (2010) (codified at 12 U.S.C. § 5371).
7 *Id.*
8 Pub. L. 113-279, 128 Stat. 3017 (2014).
9 84 Fed. Reg. at 57246.
10 *Id.* at 57275.

comply with Section 171, the Board need only determine that its capital standards for ISLHCs satisfy Section 171's requirements. We believe the BBA framework has been well designed to meet Section 171's requirements, and therefore there is no need for the Board to apply a separate capital calculation framework to ISLHCs.

Indeed, the Board itself states that it designed the BBA framework specifically "to produce a consolidated risk-based capital requirement that is not less stringent than the results derived from the Board's banking capital rule."[11] We believe this statement demonstrates why it is clear that by complying with the requirements of the NPR's BBA framework, an ISLHC would also be in compliance with the minimum requirements of Section 171. Therefore, the Board should not require entities that satisfy the BBA framework to conduct separate and additional Section 171 Calculations. Rather, we urge the Board to permit compliance with the BBA framework to constitute compliance with Section 171, consistent with congressional intent and the 2014 Amendments.

B. <u>If the Board selects one of the two proposed alternatives for deducting insurance subsidiary assets from an entity's Section 171 Calculations, TIAA recommends Option 2 (applying a 400 percent risk weighting to investment in insurance subsidiaries)</u>.

If the Board decides to maintain its requirement that ISLHCs conduct separate Section 171 Calculations, the Board has proposed two alternative approaches to the regulatory capital treatment of an ISLHC's equity investment in subsidiary insurers.[12] As discussed above, the first alternative allows the holding company to deduct the aggregate amount of its outstanding equity investment in its subsidiary state- and certain foreign-regulated insurers from its common equity tier 1 capital elements. Under the second alternative, the holding company could include in its risk-weighted assets the aggregate amount of its outstanding equity investment in state- and foreign-regulated insurance subsidiaries and affiliates, and assign to these assets a 400 percent risk weight. Acknowledging the potential drawbacks to each approach, the Board invites comment on these suggested alternatives.

TIAA recommends that the Board maintain both approaches as alternatives for ISLHCs to choose to exclude insurance operations from Section 171 Calculations. Doing so would allow ISLHCs to use the method that will result in the most appropriate calculations for their organization. However, if the Board decides to adopt only one method in a final rulemaking, TIAA urges the Board to retain Option 2, which allows a holding company to apply a 400 risk weight to its equity investment in its insurance subsidiaries. As the Board itself notes in the NPR,[13] Option 2 is consistent with the Board's approach in its regulatory capital rule for banks (the "Banking Capital Rule"),[14] which applies a 400 percent risk weight to any equity exposure that is not publicly traded.[15] For purposes of competitive equality, we would urge

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[11] *Id.* at 57245.
[12] *Id.* at 57247.
[13] *Id.*
[14] *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Capital Adequacy, Transition Provisions, Prompt Corrective Action, Standardized Approach for Riskweighted Assets, Market Discipline and Disclosure Requirements, Advanced Approaches Risk-Based Capital Rule, and Market Risk Capital Rule*, 78 Fed. Reg. 62018, 62173 (Oct. 11, 2013), *available at*: https://www.govinfo.gov/content/pkg/FR-2013-10-11/pdf/2013-21653.pdf.
[15] *Id.* at 62197.

the Board to take the approach set forth in Option 2, which would ensure that ISLHC investments in regulated insurance subsidiaries are subject to the same capital treatment as banks' equity investments under the Banking Capital Rule.

IV. TIAA respectfully requests that the Board clarify the definition of an "insurance savings and loan holding company."

The NPR's definition of "insurance savings and loan holding company" should be clarified to reflect the fact that not all prospective top-tier ISLHCs are required to prepare consolidated financial statements. The NPR defines an "insurance savings and loan holding company" as "(1) a top-tier savings and loan holding company that is an insurance underwriting company; or (2)(i) a top-tier savings and loan holding company that, as of June 30 of the previous calendar year, held 25 percent or more of its total consolidated assets in subsidiaries that are insurance underwriting companies (other than assets associated with insurance underwriting for credit risk). . ."[16] The second part of this definition assumes that all top-tier ISLHCs prepare consolidated financial statements and can use them to demonstrate that 25 percent or more of their total consolidated assets are in insurance underwriting company subsidiaries. Without clarification, this definition could be interpreted as requiring the preparation of financial statements in accordance with Generally Accepted Accounting Principles ("GAAP") by an insurance company, contrary to 12 U.S.C. 5371(c)(3)(A), which prohibits the Board from imposing such a requirement under authority of Section 171 or HOLA. We believe that the Board did not intend such a result.

To address this issue, we suggest that the Board utilize the approach it took in Section 246.3(a)(2)(ii) of Regulation TT.[17] Specifically, we urge the Board to allow a top-tier ISLHC to calculate an estimate of its total consolidated assets and the assets of its insurance underwriting subsidiaries to demonstrate that it satisfies the "25 percent or more" standard of the "insurance savings and loan holding company" definition. Such a clarification could be added as a footnote to subsection 2(i) of the definition of "insurance savings and loan holding company" and simply state: "If a savings and loan holding company does not prepare consolidated statements, such company shall use the estimation approach authorized by Section 246.3(a)(2)(ii) of Regulation TT to estimate its total consolidated assets and investment in insurance underwriting company subsidiaries for purposes of demonstrating that it satisfies this '25 percent or more' requirement."

V. The Board should adjust the minimum capital requirement and capital buffer for ISLHCs under the BBA framework to follow the methodology it has chosen to achieve equivalency with bank capital requirements rather than adding the substantial "margin of safety" it has proposed.

TIAA commends the Board for the thoroughness and thoughtfulness of its approach in developing a scaling mechanism to establish comparable capital assessment methodologies for the insurance and banking sectors. We support the Board's proposed use of the historical probability of default ("PD") scaling method as an effective approach to

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16 *Id.* at 57275.
17 12 CFR § 246.3(a)(2)(ii).

establishing comparability between capital requirements for bank holding companies and ISLHCs.

Given the rigor of the Board's approach to developing a methodologically sound scaling method, we urge the Board to faithfully apply the results of its proposed PD scaling mechanism. However, instead of doing so, the Board has proposed to add a substantial cushion to the required BBA ratio generated by the PD scaling method, in addition to the proposed capital conservation buffer that the Board is also proposing to require ISHLCs to meet.

Straightforward application of the PD scaling methodology to establish comparable bank and insurance capital requirements would result in a required core BBA ratio of 160 percent to equate to the Board's 8 percent bank capital requirement. The proposed core BBA ratio of 250 percent (in addition to a 235 percent capital conservation buffer), however, is 90 percentage points (55 percent), higher than the model-generated result. If the Board has developed a rigorous and statistically sound methodology, which we believe it has, it should follow it rather than adding an additional cushion of more than 55 percent. If the proposed methodology is not sound, it should not form the basis for the proposed capital requirements for ISHLCs.

The Board's explanation in the NPR for the decision to add an additional 55 percent cushion to the model's results is cursory and conclusory and does not provide adequate opportunity for commenters to analyze and in turn comment on the Board's rationale. The following represents the entirety of the explanation to increase the core BBA ratio from the model-generated result of 160 percent to the NPR's 250 percent proposal:

> In light of the Board's supervisory objectives and authorities in accordance with U.S. law, the Board proposes to require a minimum BBA ratio of 250 percent. The Board determined this minimum threshold by first translating the minimum total capital requirement of 8 percent of risk-weighted assets under the Board's banking capital rule to its equivalent under NAIC RBC. The Board then added a margin of safety to account for factors including any potential data or model parameter uncertainty in determining scaling parameters and an adequate degree of confidence in the stringency of the requirement. The Board notes that the proposed minimum ratio, 250 percent, aligns with the midpoint between two prominent, existing state insurance supervisory intervention points, the ''company action level'' and ''trend test level'' under state insurance RBC requirements.[18]

The Board's brief explanation surprisingly does not even mention that the PD scaling method generates a National Association of Insurance Commissioners ("NAIC") risk-based capital ("RBC") ratio of 160 percent. The explanation simply states that the Board first translated the banking requirement "to its equivalent under NAIC RBC" and "then added a margin of safety" without noting the massive magnitude of the 55 percent (90 percentage point) increase to achieve the proposed the margin of safety.

To the extent the Board feels that such a substantial increase from the equivalent result generated by the model deemed most appropriate by the Board is warranted to account for

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[18] 84 Fed. Reg. at 57261.

"any potential data or model parameter uncertainty," it should be noted that it is equally likely that the 160 percent ratio generated by the Board's proposed scaling model results in a capital requirement for insurance companies that is already significantly more stringent than an 8 percent capital requirement under the Board's Banking Capital Rule. By adding an additional 90 percentage points to the modeled result, the Board risks further exacerbating the stringency of the proposed capital requirements for the insurance sector relative to the banking sector.

The NPR also notes that the proposed 250 percent minimum ratio aligns with the midpoint between two prominent, existing state insurance supervisory intervention points, the ''company action level'' and ''trend test level.'' The NPR again fails, however, to explain any significance or appropriateness from a policy perspective of this serendipitous fact. It is equally true, for example, that the 160 percent result actually generated by the Board's proposed model falls between two equally prominent, existing state insurance supervisory intervention points, the "authorized control level" (100 percent) and "company action level" (200 percent). The model-generated 160 percent result also notably falls 10 percentage points higher than another prominent state insurance supervisory intervention point, the 150 percent "regulatory action level." Given that the Board's analysis is based on a historical comparative analysis of authorized control level capital for insurance companies and bank capital requirements for banking companies, we respectfully submit that the most relevant proposed minimum capital requirement comparison for purposes of the NPR is the model-generated result that falls 10 percentage points higher than the midpoint between the authorized control level and the company action level.

We respectfully propose that the Board should rely on the results generated by its proposed scaling model to develop an outcome that is most likely to reasonably achieve equivalency between banking and insurance capital requirements, which results in a core BBA ratio of 160 percent. With respect to the Board's concerns about the "adequate degree of confidence in the stringency of the requirement," the Board's scaling methodology analysis acknowledges that "the insurance regime's conservative accounting rules lead to a conservative calculation of available capital."[19] The analysis continues to identify reasons why the insurance sector's capital framework results in a conservative approach to available capital and the resulting lower amount of required capital in the insurance context to achieve comparable outcomes with banking requirements:

> These rules set life insurance reserves at above the best-estimate level, don't allow P&C carriers to defer acquisition expenses on policies, and don't give any credit for certain types of assets. Because of this conservative calculation of available capital, the required capital calculation is relatively lower with ACLR RBC translating to only about 1 percent of RWA.[20]

The relative conservativeness of the insurance regime in the specific context of the Board's proposed PD scaling method is further reflected by the Board's acknowledgment in its

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[19] *Comparing Capital Requirements in Different Regulatory Frameworks*, Board of Governors of the Federal Reserve System, p. 10 (Sep. 2019), *available at*: https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20190906a1.pdf.

[20] *Id.*

analysis that "[b]anking organizations have been more affected by past government support," whereas "[o]n the insurance side, government support was much less extensive."[21] The results generated by the Board's proposed PD scaling methodology accurately reflect the conservatism of the insurance regime, without effectively needing to penalize insurance companies by adding the substantial additional proposed "margin of safety." We therefore respectfully submit that 160 percent is the appropriate level for the required core BBA ratio.

> Eliminating or lowering the capital conservation buffer would provide an alternative way to ensure compliance with Section 171 of the Dodd-Frank Act without imposing more onerous capital requirements on insurance companies than on banks.

We recognize the Board's goal of implementing ISHLC capital requirements that meet the requirements of Section 171 of the Dodd-Frank Act. However, we do not understand how the NPR's unexplained, generalized approach to picking 250 percent as the appropriate level for the minimum required capital ratio for ISHLCs provides the Board, the public, and impacted companies with the "adequate degree of confidence in the stringency of the requirement."[22] To the extent that the Board believes that adding a 90 percentage point, or 55 percent, cushion to the *core* BBA model-generated ratio helps assure that Section 171 has been satisfied, the Board should consider instead lowering, or even eliminating pending further analysis, the required amount of the proposed capital conservation buffer.

Section 171 does not require the Board to impose a capital conservation buffer requirement on ISLHCs. Rather, the Board has discretion to determine whether to impose a capital conservation buffer on ISLHCs at all, and if it does, what the amount of the required minimum buffer should be. The Board explains in the NPR that it has decided to adopt a buffer for ISLHCs "to encourage better capital conservation by supervised firms and enhance the resiliency of the financial system. . ."[23] We believe the Board could promote financial resiliency more effectively by applying a capital conservation buffer to ISLHCs that is tailored to reflect the business of insurance. The buffer proposed in the NPR is based on bank capital requirements; however, we believe it is inappropriate to apply a bank-based capital conservation buffer to insurers, given their different business models and asset-liability compositions. We suggest the Board should not adopt a proposed buffer until it develops one that appropriately reflects the business and risks of insurance.

Even if the Board decides not to develop an insurance-specific capital conservation buffer for ISLHCs, we believe the buffer proposed in the NPR should be lowered to prevent it from being more onerous than the capital conservation buffer applicable to banks. The NPR currently proposes a capital conservation buffer for ISLHCs of 235 percent. In combination with the proposed 250 percent core BBA requirement, this results in an overall minimum capital requirement of 485 percent. Using the PD scaling method to determine equivalency with bank capital requirements, the combined BBA requirement of 485 percent translates to a bank capital ratio of 11.44 percent. This would result in a requirement for insurance companies that would be nearly a full percentage point higher than the 10.5 percent risk-weighted assets ("RWA") ratio required by the Banking Capital Rule. By contrast, converting the 10.5 percent bank capital requirement into its equivalent amount under NAIC RBC would

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21 *Id.* at 11.
22 84 Fed. Reg. at 57261.
23 *Id.*

result in a minimum combined required ratio of 396 percent, almost 90 percentage points lower than the proposed combined 485 percent requirement.

Therefore, if the Board retains a capital conservation buffer in the final rule, we respectfully propose that the Board lower the capital conservation buffer requirement by at least 90 percentage points from 235 percent to 145 percent. At 145 percent, the capital conservation buffer would still represent an incremental 58 percent requirement on top of the core BBA proposed minimum ratio of 250 percent. (The buffer would of course be even higher as a percentage of the core BBA ratio to the extent the Board considers our recommendation to impose a core requirement that is more consistent with the results suggested by its PD model.) This would still result in a significantly higher percentage of required capital conservation buffer for insurance companies relative to core capital requirements than is required under the Banking Capital Rule. By leaving the core BBA capital requirement at 250 percent (or any amount higher than 160 percent), the Board will have imposed a core capital requirement on insurance companies that is likely far more stringent than the requirement for bank holding companies, and that amply satisfies Section 171. With a core BBA requirement of 250 percent and a 145 percent capital conservation buffer, the resulting combined ratio of 395 percent would actually be almost exactly equivalent to the PD scaling method's model-generated result of 396 percent equivalency to the 10.5 percent RWA requirement under the Board's Banking Capital Rule. It would also be almost twice as high as the company action level capital requirements under NAIC RBC.

VI. <u>The Board should not require ISLHCs to apply PBR valuation methodologies to insurance products</u>.

In section VI.B.3 of the NPR, the Board notes that its proposed BBA framework "contains adjustments to address permitted practices, prescribed practices, or other practices," including "an adjustment to remove the effects of any grandfathering or transitional measures under an applicable capital framework in determining capital requirements."[24] Footnote 53 of the NPR clarifies that "one such adjustment that is relevant is the use of Principle-Based Reserving (PBR) on business that is currently grandfathered."[25] It is our understanding that the Board intends for ISLHCs to apply the NAIC's PBR valuation methodology to all insurance products (including in-force products) for which the NAIC has implemented a PBR valuation methodology, despite the fact that the NAIC's methodology only applies to products issued after a certain date.

We believe the proposed retroactive application of PBR methodologies to insurance products is inappropriate, particularly given that the retroactive application of such methodologies would be unduly burdensome and would require insurers to perform a theoretical analysis that they are not required to do for any other regulatory purpose. Specifically, we believe that requiring life insurers to apply a PBR methodology to grandfathered life insurance policies would contradict the Board's goal of aligning federal capital standards for ISLHCs with the requirements of state insurance regulators, as insurers are not required to do so under state insurance regulatory regimes. The grandfathering of life insurance policies is not a transition measure; rather, it is a recognition that little

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[24] *Id.* at 57256.
[25] *Id.* at 57253.

supervisory benefit would be achieved by applying a PBR methodology to these in-force policies. We recognize the Board's desire to have minimal variation in calculation methodology and to avoid regulatory arbitrage. However, neither of these goals would be served by retroactive application of PBR given that (a) only the Board is proposing to require retroactive application, defeating uniformity of approach, and (b) the risk of regulatory arbitrage is eliminated given that any new policies issued would be subject to PBR.

If the Board is not willing to follow the lead of state insurance supervisors with respect to the application of PBR methodologies to grandfathered life insurance policies, the Board should at least exclude companies with *de minimis* current and future exposure to life insurance products from its proposed PBR requirements. Specifically, where life insurance policies represent an immaterial portion of a company's overall business, and the company no longer sells new life insurance policies (and has no plans to do so in the future), we believe the required application of PBR methodologies to the company's in-force life insurance policies would be particularly inappropriate. We would urge the Board to permit such companies to refrain from applying a retroactive PBR valuation methodology to their life insurance products.

VII. <u>The Board should recalculate its limit on tier 2 capital to make it consistent with banking capital requirements</u>.

The NPR's proposed BBA framework "would limit the inclusion in the BBA of instruments meeting the criteria for tier 2 instruments under the Board's banking capital rule, but not meeting the banking capital rule's criteria for common equity tier 1, to 62.5 percent of required capital after aggregating to the level of the top-tier parent of the insurance depository institution holding company's enterprise."[26] The Board has acknowledged its intention to set a limit on tier 2 capital for ISLHCs that corresponds to the Banking Capital Rule. The preamble to the NPR explains that "the firm's tier 2 capital, held in the amount of 62.5 percent of the top-tier parent's building block capital requirement, would be one-fourth of available capital at the minimum requirement under the Board's banking capital rule, corresponding to 2 percent of risk-weighted assets in the context of the Board's banking capital rule."[27] However, we believe that the 62.5 percent limit on tier 2 capital for ISLHCs does not in fact align with the requirements of the Banking Capital Rule.

Applying the scaling formula in the NPR,[28] the 62.5 percent limit proposed for ISLHCs would equate to only 0.66 percent of risk-weighted assets in the context of the Banking Capital Rule – not 2 percent, as the NPR indicates. This means that banks are permitted to hold up to 25 percent of their total required capital in tier 2 capital under the Banking Capital Rule, but the NPR would restrict an ISLHC to holding no more than 7.4 percent of its required capital under the BBA framework in tier 2 instruments. Not only does this create an unfair competitive advantage for banks, it is in direct conflict with the Board's stated goal of designing a tier 2 capital limit for ISLHCs that aligns with the Banking Capital Rule. Therefore, we recommend that the Board recalculate a tier 2 capital limit for ISLHCs that is equivalent to the limit applicable to banks, using the proposed scaling methodology described in the NPR.

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26 84 Fed. Reg. at 57272.
27 *Id*. at 57260, note 75.
28 *Id*. at 57281.

VIII. **<u>The Board should give ISLHCs credit for using additional tier 1 capital</u>.**

The NPR does not establish a separate category of capital corresponding to the additional tier 1 capital described in the Banking Capital Rule. The Board notes in the NPR that "the BBA, as proposed, does not reflect or utilize the criteria for additional tier 1 capital under the Board's banking capital rule," because "in the Board's supervisory experience, the incidence of insurers utilizing capital instruments that meet the criteria of additional tier 1, but not the criteria of common equity tier 1 is not common, and when utilized, does not frequently represent a material proportion of the insurer's capital."[29]

While insurers may not have utilized additional tier 1 capital at high rates historically, we believe the NPR should provide for such use in the future. Neglecting to establish a separate category of additional tier 1 capital in the NPR places ISLHCs at a competitive disadvantage to banks, as insurers would be limited to meeting their minimum capital requirement using common equity or retained surplus. ISLHCs would also be forced to satisfy 100 percent of their minimum capital buffer requirement under the NPR using common equity or retained surplus. To address this disparity, we urge the Board to give ISLHCs credit for using additional tier 1 capital at the same rate that banks are permitted to do so under the Banking Capital Rule.

IX. **<u>ISLHCs should not be required to complete Schedule I of Form FR Q-1 for every entity in their organization, as doing so would be unduly burdensome and unnecessary to report their organization's applicable capital requirements</u>.**

The NPR includes a proposal to implement a new reporting form titled "Capital Requirements for Board-Regulated Institutions Significantly Engaged in Insurance Activities," or Form FR Q-1, for use in connection with the BBA framework.[30] To complete Schedule I of Form FR Q-1 as currently proposed, ISLHCs would be required to provide information about every entity in their organization, including each entity's regulatory and applicable capital framework, accounting basis, assets, and liabilities.

We are concerned that ISLHCs with a large number of entities in their organization may be required to spend an exorbitant amount of time completing Form FR Q-1; in fact, we have estimated that it could take close to 350 hours annually for certain ISLHCs to provide the detailed information requested in the form. This is not only due to the sheer number of entities that an ISLHC may need to cover, but also because it may be difficult for an ISLHC to obtain the underlying data for every entity and reconcile it to a standard format in Schedule I. For example:

- An ISLHC may not receive underlying subsidiary trial balances for all lower-tier entities within its organization. Instead, the ISLHC may receive consolidated trial balances at the upper-tier entity level, which would include several underlying trial balances for lower-tier entities that would be very difficult to separate and attribute and would require additional data requests.

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29 *Id*. at 57260, note 76.
30 *Id*. at 57269.

- The underlying subsidiary trial balances for lower-tier entities might not include consolidation or elimination adjustments that are made at the tier 1 level. Without making consolidation adjustments to the assets and liabilities of these lower-tier entities, total assets and liabilities could be inflated due to double counting.
- The underlying subsidiary trial balances of lower-tier entities would include 100 percent of each entity's balance sheet and would not take into account ownership percentages below 100 percent at higher-tier subsidiary levels. This would ultimately cause assets and liabilities to be overstated.
- The underlying subsidiary trial balances of lower-tier entities might be calculated using a non-US GAAP accounting basis (*e.g.*, IFRS or local country GAAP), whereas tier 1 data is adjusted to reflect US GAAP.

We do not believe the Board desires or intends ISLHCs to spend hundreds of hours annually to complete Schedule I of Form FR Q-1. Moreover, we believe ISLHCs can provide sufficient disclosures about the capital requirements that apply to their organization by filling out Schedule I for their tier 1 entities only. The Board of course retains the ability to obtain any additional information from ISLHCs through its normal supervisory process. For these reasons, we would respectfully request that the Board permit ISLHCs to complete Schedule I of Form FR Q-1 with respect to their tier 1 entities only. Such an approach would provide the Board with sufficient information about ISLHCs' applicable capital requirements and avoid the unnecessary burden associated with preparing Schedule I for entities below the tier 1 level.

X. **The Board should eliminate the audit requirement from the Form FR Q-1 attestation.**

Proposed Form FR Q-1 includes an attestation that must be signed by an ISLHC's Chief Financial Officer or equivalent senior officer.[31] Among other things, the attestation requires the relevant officer to attest that the ISLHC has implemented internal controls over the reporting of Form FR Q-1 data and that those controls are audited at least annually by the ISLHC's internal audit or compliance staff and assessed regularly by the ISLHC's management. This provision would require ISLHCs to put in place new controls over the reporting of Form FR Q-1 data or leverage existing controls in a new manner. Requiring ISLHCs to additionally audit those controls on an annual basis would increase compliance costs without significantly increasing the quality or reliability of Form FR Q-1 data. Given that a senior officer of each ISLHC is required to attest to the accuracy of the firm's FR Q-1 data and the existence of relevant internal controls, we believe the audit requirement is unnecessary and overly burdensome. ISLHCs should be allowed to determine the appropriate approach and frequency for auditing the controls consistent with their existing audit planning procedures. As such, we respectfully request that the Board eliminate the audit requirement from the Form FR Q-1 attestation.

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31 Form FR Q-1 Attestation Cover Page*, available at*: https://www.federalreserve.gov/reportforms/formsreview/FR%20Q-1%20Attestation%20Cover%20Page.pdf.

XI. Conclusion

TIAA commends the Board for its thoughtful approach to formulating capital standards for ISLHCs. It is crucial that the capital regime for ISLHCs is carefully designed and well-tailored to the business of insurance, and we applaud the Board for proposing a BBA framework that addresses the unique needs and qualities of ISLHCs. We appreciate the opportunity to provide our thoughts on how that approach might be further refined and improved, and we hope our suggestions are helpful as the Board works to finalize its proposal. We would welcome the opportunity to engage further on any aspects of the NPR.

Sincerely,

Bret C. Hester

Bret C. Hester