Chief Counsel's Office
Attention: Comment Processing
Office of the Comptroller of the Currency
400 7th Street SW, Suite 3E-218
Washington, DC 20219

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

James P. Sheesley
Assistant Executive Secretary
Attention: Comments/Legal OES (RIN 3064-AF29)
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

January 16, 2024

RE: Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, Docket ID OCC-2023-008 (Office of the Comptroller of the Currency) / Docket No. R-1813, RIN 7100-AG64 (Federal Reserve System) / RIN 3064-AF29 (Federal Deposit Insurance Corporation)

To Whom It May Concern:

The Reinsurance Association of America ("RAA"), on behalf of and in coordination with its members, is pleased to provide its comments to the Office of the Comptroller of the Currency (the "OCC"), the Board of Governors of the Federal Reserve System (the "Federal Reserve System"), and the Federal Deposit Insurance Corporation (the "FDIC" and collectively, the "Agencies") with respect to the July 27, 2023, notice of proposed rulemaking (the "Proposal") intended to revise the capital requirements applicable to large banking organizations and to banking organizations with significant trading activity, the U.S. implementation (such rules, the "U.S. Basel III Regulations") of the remaining elements of the Basel III agreement (known as the "Basel III Endgame") on

international capital standards issued by the Basel Committee on Banking Supervision (the "Basel Framework").[1]

The RAA is the leading trade association of property and casualty reinsurers doing business in the United States. RAA membership is diverse, including reinsurance underwriters and intermediaries licensed in the United States and those that conduct business on a cross border basis. The RAA also has life reinsurance affiliates and insurance-linked securities (ILS) fund managers and market participants that are engaged in the assumption of property/casualty risks. The RAA represents its members before state, federal and international bodies.

EXECUTIVE SUMMARY

- The Agencies' Proposal included a significant increase in capital requirements, in particular for residential mortgage lending, which will, at a minimum:
    1) Limit lending;
    2) Result in increased borrowing costs for U.S. businesses and consumers;
    3) Increase lending by non-banks outside of the regulatory perimeter; and
    4) Potentially have an adverse effect on financial stability, increasing risk to U.S. taxpayers.

- To mitigate these undesirable consequences, the RAA recommends and requests that, in advance of the Agencies' final rule implementing the Basel III Endgame ("Final Rule"), the Agencies revise the Proposal to include clarifying language regarding a bank's ability to transfer credit risk to prudentially regulated, well-capitalized property and casualty insurance and reinsurance companies ("insurance companies") and receive significant capital relief as a result, specifically to:
    1) Explicitly permit prudentially regulated, well-capitalized insurance companies to provide credit protection to banks by clarifying that insurance companies are "eligible guarantors," as well as making certain clarifications to the definition of an "eligible guarantee"; and
    2) Adopt tiered risk weights to provide meaningful capital relief to banks for transferring credit risk to prudentially regulated, well-capitalized insurance companies.

- While the Basel Framework's credit risk mitigation provisions provide that credit protection given by "prudentially regulated financial institutions" with a lower risk weight than the counterparty may be recognized under the standardized approach and specify "prudentially regulated insurance companies" as an example of such an institution,[2] neither the U.S. Basel III Regulations nor the Proposal permit this option.

---

[1] Office of the Comptroller of the Currency, Federal Reserve System and FDIC, Regulatory capital rule: Amendments applicable to large banking organizations and to banking organizations with significant trading activity, 88 Fed. Reg. 64028 (Sept. 18, 2023).

[2] Basel Framework CRE22.76(1), fn. 11. We acknowledge that neither the EU Capital Requirements Regulation (the "EU CRR") nor the UK "onshored" Capital Requirements Regulation (the "UK CRR") include insurance companies (prudentially regulated or otherwise) in its list of specifically eligible guarantors. However, in accordance with the approach in the Basel Framework, eligible guarantors under both the EU CRR and the UK CRR includes corporate entities that have a credit assessment by an "eligible credit assessment institution." *See* EU CRR Art. 201(1)(g)(1);

- RAA believes that adopting these changes will: enhance the safety and soundness of the U.S. banking system; preserve, for example, access to affordable credit for small businesses and manufacturers and housing finance options for first-time homebuyers, people of color, residents of rural areas, and people with low and moderate incomes; allow banks to better manage balance-sheet risk; enhance financial stability; and protect taxpayers.

The RAA has included in this comment letter detailed proposed changes to achieve the above-mentioned objectives and asks that the Agencies include these in the Final Rule.

We urge you to consider these comments as a complement to those submitted by individual RAA members.

INTRODUCTION TO INSURANCE/REINSURANCE INDUSTRY

Since the 15th century, reinsurance, or "…insurance for insurance companies…," has been "…an essential tool insurance companies use to manage risk and the amount of capital they must hold to support those risks," specifically to "…support the issuance of new policies, to minimize fluctuations in loss experience, and to limit and diversify individual and portfolio risks, particularly in the case of catastrophes and natural disasters."[3] Today, in the United States, private and public sector use of reinsurance underpins the U.S. economy.[4]

1. Insurance Companies are Highly Regulated

As the Agencies note in the Proposal, "[t]he absence of prudential regulation…lead[s] to an increase in the credit risk of [non-bank financial] entities in the form of a greater risk of default in stress periods."[5] By contrast, insurance companies, which *are* prudentially regulated, present a lower risk of default in stress periods and thus lower credit risk to the banking system.

Domestic Insurance Regulation. U.S. insurance companies are subject to comprehensive state-level prudential regulation of each insurer entity within an insurance group. The National Association of Insurance Commissioners ("NAIC"), a national body governed by the chief insurance regulators of each U.S. state, territory, and the District of Columbia, establishes national standards for the regulation of the insurance industry. While the NAIC does not have independent lawmaking authority, states adopt NAIC model laws and standards in substantially similar form,

---

UK CRR Art. 201(1)(g)(1). It would be reasonable to assume that many externally rated insurance companies qualify as eligible guarantors for purposes of the EU CRR and the UK CRR on this basis. In the United States, Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") required the Agencies to remove all references to external ratings from their regulations, including capital adequacy requirements, and, therefore, the U.S. Basel III Regulations do not take external ratings into account in defining who may be deemed an eligible guarantor.

[3] National Association of Insurance Commissioners, "Reinsurance," https://content.naic.org/cipr-topics/reinsurance (October 18, 2023).

[4] U.S. Department of the Treasury, "The Breadth and Scope of the Global Reinsurance Market and the Critical Role Such Market Plays in Supporting Insurance in the United States," https://home.treasury.gov/system/files/311/FIO%20-Reinsurance%20Report.pdf (December 2014).

[5] Proposal, *supra* note 1, at 64063.

ensuring uniform implementation across and among the states. This is because, for a state's insurance department to be accredited by the NAIC, the state must have adopted substantially similar NAIC model laws, regulations and standards considered to be "basic building blocks for effective financial solvency regulation."[6]

Moreover, while the states have insurance holding company laws and regulations, state insurance company regulation has a particular focus on the supervision of each insurance legal entity (which is walled off from its holding company or other affiliates). This robust regulatory framework, among other factors, has resulted in a significant reduction in insurer impairments that could lead to insolvency. This has proven itself to be a worthy countercyclical element of insurer solvency during major market downturns and loss events (discussed further in the next section).

Notably, insurance companies must comply with stringent capital regulations. Risk-based capital ("RBC") standards have been designed for each type of insurer (*i.e.*, property and casualty ("P&C"), life, health) under the NAIC Risk-Based Capital for Insurers Model Act (as adopted – in the same or substantially similar form – by each state). For example, a P&C insurer's RBC formula accounts for asset risk, credit risk, underwriting risk and business risk.[7] These risks are assessed and weighted according to the specified formula to determine the insurer's RBC ratio. On an annual basis, each insurer prepares and submits to its relevant state insurance regulator(s) and the NAIC a report of its RBC levels based on this calculation and as compared to the insurer's total adjusted capital (as calculated under the formula) and authorized control level capital.[8] If the insurer's reported RBC ratio is inadequate under the standards set forth by the NAIC (as adopted by the state), the insurer's regulator may require submission of an action plan by the insurer or may have to take corrective action over the insurer.[9] This could include, in certain circumstances, the state regulator taking control of the insurer.

Investments by insurers using their surplus capital are also subject to strong regulatory limitations. In determining the financial condition of an insurer, and for purposes of the RBC calculations and other regulatory requirements, state law generally distinguishes between admitted and non-admitted assets.[10] Admitted assets, which are included in the calculation of an insurer's surplus capital, are those that are more secure, readily available to satisfy policyholder obligations, and are thus afforded more favorable RBC treatment.[11] State insurance law also generally imposes limitations on admitted assets in order to avoid over-concentration.[12] Given that insurers cannot count non-admitted assets towards their regulatory capital requirements, insurers will typically limit their holdings of such assets.

---

[6] NAIC, Financial Regulation Standards and Accreditation Program (August 2022), https://content.naic.org/sites/default/files/inline-files/FRSA%20Pamphlet%208-2022%20.pdf, at 7.
[7] NAIC, Risk-Based Capital (RBC) for Insurers Model Act, Section 2.C, https://content.naic.org/sites/default/files/inline-files/MDL-312.pdf.
[8] *See, e.g.*, New York Insurance Law § 1324. Total adjusted capital is the sum of an insurer's statutory capital and surplus and such other items as the standards of the NAIC may provide. Authorized control level is the number determined under the RBC formula set forth under the NAIC standards.
[9] *See, e.g.*, New York Insurance Law § 74.
[10] *See, e.g.*, New York Insurance Law § 1301-1302.
[11] *See, e.g.*, New York Insurance Law § 1301.
[12] *See, e.g.*, New York Insurance Law § 1409.

In addition, state insurance regulators have regulatory measures in place to ensure that insurance companies have sufficient liquidity to meet their obligations and maintain financial stability. Liquidity risk refers to the potential for an insurance company to encounter difficulties in meeting its short-term obligations due to an inability to convert assets into cash quickly enough. To ensure the stability and solvency of insurance companies, liquidity risk is regulated through various measures.

Insurance regulators may require insurance companies to undergo regular stress testing exercises. These tests evaluate the company's ability to withstand adverse liquidity events, such as natural catastrophes, a sudden surge in policyholder withdrawals or a significant decrease in market liquidity. The NAIC requires annual filing of an Own Risk and Solvency Assessment (ORSA) by larger (re)insurers, which includes a prospective solvency assessment, scenario analysis and stress testing to ensure material risks do not adversely impact its solvency position. By simulating various scenarios, regulators can assess the adequacy of an insurance company's liquidity risk management practices. These plans outline the actions the company would take in the event of a liquidity crisis, such as accessing emergency funding sources or implementing liquidity preservation measures.

Following the Global Financial Crisis (GFC), private mortgage insurers, their state regulators, and the government-sponsored entities Fannie Mae and Freddie Mac (collectively, the "Enterprises"), which are regulated by the Federal Housing Finance Agency ("FHFA"), have enhanced capital requirements, as well as risk-management and policy certainty among other things, as a result of reforms adopted for private mortgage insurers. Private mortgage insurers are subject to a specifically tailored and comprehensive set of loss reserving requirements designed to ensure that such insurers retain enough capital to pay claims when the economic cycle experiences a downturn. Specifically, private mortgage insurers are required to contribute 50% of earned premium to a contingency reserve to be held for 10 years. Consistent with a NAIC model law, private mortgage insurers provide state insurance regulators with an annual Own Risk and Solvency Assessment (ORSA) to demonstrate that the insurer can meet policyholder obligations in the event of a catastrophic loss event (with estimates which could be based on economic scenarios such as the Federal Reserve System's Comprehensive Capital Analysis and Review (CCAR) test and a GFC replay). Private mortgage insurers also are subject to the Enterprises' Private Mortgage Insurer Eligibility Requirements (PMIERs) to be able to insure Enterprise-financed mortgage loans, including capital, investment policy, risk and operational standards. Due to strict investment limitations, private mortgage insurers generally minimize exposure to wrong-way risk (*i.e.*, that which can arise from investing in assets issued by the industry in which the guaranteed counterparty operates). Post GFC, private mortgage insurers have substantially increased the use of reinsurance to better diversify and manage risk. Moreover, capital distributions by such insurers also are subject to regulatory oversight.

Foreign Insurance Regulation. Foreign insurance companies in certain jurisdictions are also subject to comparable regulation, which we believe is appropriately reflected in our recommendations below. Section 502 of the Dodd-Frank Act authorizes the Secretary of the Treasury and the U.S. Trade Representative to jointly negotiate a "covered agreement" on behalf of the United States with one or more foreign governments, authorities or other regulatory entities. Such an agreement "relates to the recognition of prudential measures with respect to the business

of insurance or reinsurance that achieves a level of protection for insurance or reinsurance consumers *that is substantially equivalent to the level of protection achieved under state insurance or reinsurance regulation*" (emphasis added).[13] To date, the United States has entered into such agreements with the European Union (2017) and the United Kingdom (2018).

Furthermore, the NAIC recognizes certain non-U.S. jurisdictions as "reciprocal jurisdictions" in accordance with the NAIC Credit for Reinsurance Model Law and Regulation. The NAIC has stated that—

> The standard for qualification of a jurisdiction is that the NAIC must reasonably conclude that the jurisdiction's reinsurance supervisory system achieves a level of effectiveness in financial solvency regulation that is deemed acceptable for purposes of reinsurance collateral reduction, that the jurisdiction's demonstrated practices and procedures with respect to reinsurance supervision are consistent with its reinsurance supervisory system, and that the jurisdiction's laws and practices satisfy the criteria required of Qualified Jurisdictions as set forth in the Credit for Reinsurance Models.[14]

In light of the high standards imposed on such insurers under covered agreements and in order to be recognized as a reciprocal jurisdiction, RAA believes that non-U.S. insurance companies subject to these requirements should receive comparable treatment for bank capital relief purposes.

2. *Government Entities Have Expanded Use of (Re)Insurance CRT*

Since 2013, the reinsurance industry has transferred mortgage credit risk from the Enterprises to private sector balance sheets.[15] Prior to the GFC, the Enterprises retained 100% of the mortgage credit risk they accumulated; the concentration of credit risk on the Enterprises' balance sheets was a primary driver of their failure and ultimate conservatorship under the FHFA.[16] Under conservatorship, in 2012, the Enterprises established a credit risk transfer ("CRT") program, which "…have included CRTs via capital markets issuances…, insurance/reinsurance transactions," and other transactions – to reduce taxpayer exposure to risks arising from credit guarantees extended by the Enterprises through their normal courses of business.[17] Since then, the Enterprises have

[13] U.S. Department of the Treasury, Covered Agreements, https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/federal-insurance-office/covered-agreements.
[14] NAIC, *Process for Evaluating Qualified and Reciprocal Jurisdictions*, at 9 (Aug. 17, 2021). Currently, the NAIC reciprocal jurisdictions include all European Union member states and the United Kingdom pursuant to Dodd-Frank Act covered agreements, plus Bermuda, Japan, and Switzerland. Bermuda's status as an NAIC reciprocal jurisdiction is currently applicable only to (re)insurers of Class 3A, Class 3B and Class 4, and long-term insurers of Class C, Class D and Class E.
[15] *See, e.g.*, Freddie Mac, ACIS® Deal Documents, https://capitalmarkets.freddiemac.com/crt/reinsurance/deal-documents; Fannie Mae, CIRT Transactions and Servicing Reports, https://capitalmarkets.fanniemae.com/credit-risk-transfer/single-family-credit-risk-transfer/credit-insurance-risk-transfer/cirt-transactions-and-servicing-reports.
[16] *See, e.g.*, Don Layton, Demystifying GSE Credit Risk Transfer: Part 1 – What Problems Are We Trying to Solve, Joint Center for Housing Studies of Harvard University (January 2020), https://www.jchs.harvard.edu/sites/default/files/media/imp/harvard_jchs_gse_crt_part1_layton_2020.pdf.
[17] FHFA, Credit Risk Transfer, https://www.fhfa.gov/PolicyProgramsResearch/Policy/Pages/Credit-Risk-Transfer.aspx.

transferred a meaningful amount of credit risk to private insurers, which is a critical component of FHFA's annual scorecard for the Enterprises.[18] The success of the CRT program renewed confidence in the revised practices of the Enterprises. CRT is now structured and incentivized as part of the FHFA's "Enterprise Regulatory Capital Framework" for the Enterprises.[19] Reinsurers that regularly evaluate and partner in this risk provide objective third-party feedback of the risk, which is not only valuable to the institutions ceding the risk, but also to regulators when exercising oversight. Critically, the Enterprises' are able to access both the capital markets and the insurance and reinsurance markets, which allows the Enterprises' to optimize their capital and risk management needs.

Since 2017, the reinsurance industry also has backed the U.S. Department of Homeland Security Federal Emergency Management Agency's National Flood Insurance Program ("NFIP") and paid over $1 billion to the NFIP to help pay claims after Hurricane Harvey (2017). Since 2018, reinsurers have shared risk with the Export-Import Bank of the United States. ("EXIM") to increase trade finance, reduce taxpayer risk, and provide an additional tool to EXIM "as part of its comprehensive risk management strategy."[20] Our industry also supports several state programs in the United States. The RAA's membership includes companies across the entire value chain of mortgage, trade, and other forms of CRT, from brokers to private mortgage insurers to reinsurers.

3. (Re)insurance CRT Would Enhance Financial Stability

Reinsurance is largely uncorrelated to financial markets in a time of stress, as demands for payment are conditioned on a loss event specified under the reinsurance contract, which are rarely correlated with economic cycles or financial crises. The long-term character of insurance liabilities makes them virtually immune from a "run on the bank" scenario. Another reason why reinsurance is uncorrelated to financial stress is the diversification of risk. Reinsurance allows insurance companies to spread their risks across multiple insurers, who operate globally and have exposure to various geographic regions and lines of business. This diversification helps reduce the impact of localized financial stress events on the reinsurers' ability to honor their reinsurance contracts. By having a wide portfolio of risks, reinsurers are less susceptible to the financial stress experienced by the broader financial markets.

4. Banks Should Receive Credit for Transferring Risk to Prudentially Regulated, Well-Capitalized (Re)insurance Companies

RAA agrees with Vice Chair Barr that "capital is foundational to [the safety and soundness of the banking system],"[21] and we generally support the goals and objectives of the Proposal. However,

[18] *See* FHFA, 2023 Scorecard for Fannie Mae, Freddie Mae, and Common Securitization Solutions (December 2022), https://www.fhfa.gov/AboutUs/Reports/ReportDocuments/2023-Scorecard.pdf.
[19] "Enterprise Regulatory Capital Framework Prescribed Leverage Buffer Amount and Credit Risk Transfer," 87 Fed. Reg. 14764 (March 16, 2022) (12 C.F.R. pt. 1240), https://www.federalregister.gov/documents/2022/03/16/2022-04529/enterprise-regulatory-capital-framework-prescribed-leverage-buffer-amount-and-credit-risk-transfer.
[20] Export-Import Bank of the United States, "Reinsurance & Risk Sharing," https://www.exim.gov/about/special-initiatives/risk-sharing#_ftn1.
[21] Federal Reserve System, Statement by Vice Chair for Supervision Michael S. Barr, https://www.federalreserve.gov/newsevents/pressreleases/barr-statement-20230727.htm (July 27, 2023).

as drafted, the Proposal has not struck the right balance between the economic costs and benefits. The cost of the 20% capital increase required by the Proposal ultimately will be borne by bank customers, including first-time homebuyers, people of color, residents of rural areas, people with low and moderate income, manufacturers, and small businesses. We believe that the goal of increasing the safety and soundness of the banking system and an improved balance between economic costs and benefits can be better achieved, in part, by providing banks with a variety of meaningful, capital management tools, such as transferring credit risk to well-capitalized and prudentially regulated insurance companies.

While the Proposal seeks to align the U.S. Basel III Regulations with the Basel Framework in certain areas (such as treatment of "investment grade" corporate exposures), we believe that it still leaves meaningful gaps with respect to recognizing the benefits of credit risk mitigation through CRT transactions with insurance companies. These gaps not only place banks subject to those rules at a competitive disadvantage, but we believe also undermine the resiliency of the U.S. banking system by depriving U.S. banks a valuable credit risk mitigation tool through the transfer of risk to well-capitalized and prudentially regulated insurers.

PROPOSED AMENDMENTS

Under both the Basel Framework and the U.S. Basel III Regulations, banking organizations may recognize certain types of credit risk mitigants (such as guarantees and credit derivatives) to reduce their capital requirements for certain credit exposures. As the Agencies state in the Proposal, "[p]rudent use of such mitigants can help a banking organization reduce the credit risk of an exposure…."[22] To that end, in determining whether a particular guarantee or credit derivative may be recognized for risk-based capital purposes, the U.S. Basel III Regulations primarily look to (i) the creditworthiness of the guarantor and (ii) the features of the underlying contract.

Unfortunately, even though (re)insurance companies generally have a high degree of creditworthiness, and (re)insurance contracts are generally of "sufficiently high quality to effectively reduce credit risk,"[23] the U.S. Basel III Regulations neither explicitly permit (re)insurance companies to be "eligible guarantors" nor clearly permit (re)insurance contracts to be "eligible guarantees," preventing a bank from transferring credit risk on a programmatic and consistent basis to highly regulated and well-capitalized and -diversified (re)insurance companies. Furthermore, the U.S. Basel III Regulations do not provide U.S. banking institutions with capital relief for transferring credit risk to (re)insurance companies, as exposures to (re)insurance companies are treated as any other corporate exposure despite clear differences between the risks associated with exposures to (re)insurance companies and the risks associated with exposures to other types of companies and the fact that insurance companies are highly regulated entities. Accordingly, RAA strongly encourages the Agencies to adopt the following changes as part of the Final Rule.

---

[22] Proposal, *supra* note 1, at 64058.
[23] *Id.*

1. Eligible Guarantors

The Basel Framework and the U.S. Basel III Regulations permit banks to recognize "eligible guarantees" provided by "eligible guarantors" as a credit risk mitigant. However, the approach of the U.S. Basel III Regulations differs in certain key respects from that under the Basel Framework, which effectively prevents highly regulated, well-capitalized insurance companies from providing credit risk mitigation to banks on a programmatic and consistent basis.

The first prong of the definition of "eligible guarantor" in § __.2 of the U.S. Basel III Regulations specifically includes, among others, depository institutions, bank holding companies, savings and loan holding companies, credit unions, foreign banks and qualifying central counterparties, but does not include insurance companies. The Basel Framework's credit risk mitigation provisions, on the other hand, include insurance companies by providing that credit protection given by "prudentially regulated financial institutions" with a lower risk weight than the counterparty may be recognized under the standardized approach and further specifying "prudentially regulated insurance companies" as an example of such an institution.[24]

The second prong of the eligible guarantor definition in the U.S. Basel III Regulations sets forth the criteria for eligible guarantors other than the specifically eligible guarantors listed in the first prong. This prong effectively excludes insurance companies as well:

> An entity (other than a special purpose entity):
>
> (i) That at the time the guarantee is issued or anytime thereafter, has issued and outstanding an unsecured debt security without credit enhancement that is investment grade (hereinafter referred to as the "Outstanding Investment Grade Debt Requirement");
>
> (ii) Whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees; and
>
> (iii) That is not an insurance company engaged predominately in the business of providing credit protection (such as a monoline bond insurer or re-insurer).

Insurance companies typically do not issue debt securities, investment grade, exchange traded or otherwise; instead, debt issuance and similar financing functions are performed by the insurance company's parent holding company. Thus, the insurance company itself does not meet the Outstanding Investment Grade Debt Requirement.

Similar to the Outstanding Investment Grade Debt Requirement in the U.S. Basel III Regulations, an eligible guarantor under the Basel Framework must have "securities outstanding on a recognised securities exchange." The Basel Framework's approach for other eligible guarantors, however, explicitly permits consideration of securities issued by the eligible guarantor's *parent company* (as well as those issued by the eligible guarantor itself). Specifically, "[i]n jurisdictions

[24] *See* discussion at *supra* note 2.

that do not allow the use of external ratings for regulatory purposes" (similar to the U.S.) it recognizes credit protection given by—

> Other entities, defined as "investment grade" meaning they have adequate capacity to meet their financial commitments (including repayments of principal and interest) in a timely manner, irrespective of the economic cycle and business conditions. When making this determination, the bank should assess the entity against the investment grade definition taking into account the complexity of its business model, performance against industry and peers, and risks posed by the entity's operating environment. Moreover, the following conditions will have to be met:
>
> (i) For corporate entities (or the entity's parent company), they must have securities outstanding on a recognised securities exchange;
>
> (ii) The creditworthiness of these "investment grade entities" is not positively correlated with the credit risk of the exposures for which they provided guarantees.[25]

The Proposal addresses these differences in the new "expanded risk-based approach" ("ERB Approach") under the Proposal, providing for a 65% risk weight for "investment grade" corporate exposures:

> (1) A [BANKING ORGANIZATION] must assign a 65 percent risk weight to a corporate exposure that is an exposure to a company that is investment grade and that has a publicly traded security outstanding or that is controlled by a company that has a publicly traded security outstanding.

Unfortunately, the Proposal does not address these differences in the U.S. Basel III Regulations' definition of "eligible guarantor," which is necessary to clearly permit highly regulated, well-capitalized insurance companies to provide credit risk mitigation to banks.

<u>Therefore, we urge the Agencies to address this in the Final Rule by amending the definition of "eligible guarantor" to include a "qualifying insurance company" (as defined below).</u>

A "qualifying insurance company" would be defined as a U.S. insurance company or foreign insurance company[26]:

- that at the time the guarantee is issued or anytime thereafter (i) has (or is controlled by a company that has) issued and outstanding an unsecured debt security without credit

[25] Basel Framework CRE22.76(3)(a). Note that, because the European Union and the United Kingdom *do* allow the use of external ratings for regulatory purposes, the EU CRR and the UK CRR do not contain analogous provisions.

[26] A "foreign insurance company" would be defined as any entity that is (i) organized under the laws of a foreign country, (ii) engaged in the business of insurance, (iii) supervised and regulated by a foreign insurance regulator in a manner similar to a U.S. insurance company and (iv) covered by a law of the foreign country that is designed to specifically deal with the rehabilitation, liquidation or insolvency of an insurance company.

enhancement that is investment grade *or* (ii) is investment grade and has (or is controlled by a company that has) a publicly traded security outstanding;

- in the case of a U.S. insurance company, that meets or exceeds the minimum risk-based capital, solvency capital or similar requirements established by its State insurance regulator;

- in the case of a foreign insurance company, that (i) is domiciled and licensed in a foreign country that (A) is (or is a member state of) a jurisdiction subject to a covered agreement[27] or (B) is a reciprocal jurisdiction[28] and (ii) meets or exceeds the minimum risk-based capital, solvency capital or similar requirements established by its foreign insurance regulator;

- whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees, or, if its creditworthiness is positively correlated with the credit risk of the exposures for which it has provided guarantees, that has demonstrated to the satisfaction of the applicable banking organization (in accordance with the banking organization's capital and credit-risk management policies and procedures) either (i) that it has mitigated the associated risk (such as via reinsurance) or (ii) that it has a diversified concentration risk profile, as described by the FDIC and in our attached explanatory document[29]; and

- that is not an insurance company engaged predominantly in the business of providing credit protection (such as a monoline bond insurer or re-insurer) or, if its creditworthiness is positively correlated with the credit risk of the exposures for which it has provided guarantees, that has demonstrated to the satisfaction of the applicable banking organization (in accordance with the banking organization's capital and credit-risk management policies and procedures) either (i) that it has mitigated the associated risk or (ii) that it has a diversified concentration risk profile (as described above).

2. Eligible Guarantees

To provide credit risk mitigation to banks, an eligible guarantor must provide an "eligible guarantee" that is "unconditional." The "unconditional" requirement is common across the U.S. Basel III Regulations[30], the Basel Framework, the EU Capital Requirements Regulation (CRR) and the UK CRR.

---

[27] *Covered agreement* has the meaning given that term in Section 502 of the Dodd-Frank Act, which created the Federal Insurance Office. Currently, the United States has Dodd-Frank Act covered agreements in effect with the European Union and the United Kingdom.

[28] *See supra* note 14.

[29] Generally speaking, a banking organization's or a counterparty's "concentration risk profile" is a snapshot of its overall credit exposure concentrations with respect to single counterparties, affiliated groups, industry sectors, collateral types and geographic regions at any given time. *See* FDIC Office of Inspector General, Forward-Looking Supervision 7 n.11 (Evaluation Report 18-004, August 2018). A "diversified" concentration risk profile has fewer and/or smaller concentrations of credit exposure than a concentration risk profile that is relatively undiversified.

[30] Under the U.S. Basel III Regulations, a limited exception from this "unconditional" requirement is provided for certain contingent obligations of the U.S. government or its agencies.

While the "unconditional" requirement is the same across jurisdictions, the United States is the only jurisdiction that has not provided accompanying guidance addressing whether this "unconditional" requirement applies to all conditions to the protection provider's performance (including, for example, payment of premiums and beneficiary reporting obligations) or only conditions outside the direct control of the beneficiary (for example, a "nuclear" coverage exclusion). Operational requirements under the Basel Framework clarify that a guarantee or credit derivative "must be unconditional; there should be no clause in the protection contract *outside the direct control of the bank* that could prevent the protection provider from being obliged to pay out in a timely manner in the event that the underlying counterparty fails to make the payment(s) due."[31] Following the Basel Framework's approach, the EU CRR provides that credit protection deriving from a guarantee or credit derivative shall qualify as eligible unfunded credit protection only if "the credit protection contract does not contain any clause, the fulfilment of which is *outside the direct control of the lender*, that [among other things] could prevent the protection provider from being obliged to pay out in a timely manner in the event that the original obligor fails to make any payments due."[32] The UK CRR contains identical language.[33]

<u>The RAA respectfully requests the Agencies provide this same clarity by amending the definition of "eligible guarantee" to clarify that an "unconditional" guarantee is one that includes no provision outside the direct control of the beneficiary, the non-satisfaction of which would give the protection provider the contractual right to refuse payment under the guarantee.</u>

3. *Risk-Weighing of Exposures to Insurance Companies*

Each of the U.S. Basel III Regulations, the Basel Framework, the EU CRR and the UK CRR treat exposures to insurance companies as corporate exposures, all of which are assigned a 100% risk weight.[34] The Basel Framework assigns risk weights ranging from 20% to 150% (in accordance with their "eligible credit assessment institution" ratings) to exposures to "rated" corporates in jurisdictions that allow the use of external ratings for regulatory purposes.[35]

As noted above, with respect to certain "investment grade" corporate exposures, the Proposal aligns the United States with the Basel Framework by providing for a 65% risk-weight for such exposures under the proposed ERB Approach. Specifically, the 65% risk weight would apply to "a corporate exposure that is an exposure to a company that is investment grade and that has a publicly traded security outstanding or that is controlled by a company that has a publicly traded security outstanding." Thus, an eligible guarantee provided by an insurance company that has, or

[31] Basel Framework CRE22.71(5) (emphasis added).
[32] EU CRR Art. 213(1)(c) (emphasis added).
[33] *See* UK CRR Art. 213(1)(c).
[34] The Basel Framework, the EU CRR and the UK CRR all contemplate exposures to "financial institutions" subject to certain prudential requirements being treated as exposures to banks for risk-weighting purposes. *See* Basel Framework CRE20.40; EU CRR Art. 119(5); UK CRR Art. 119(5). However, none of the three regimes define the term "financial institution" to include insurance companies. *See* Basel Framework SCO30.1; EU CRR Art. 4(1)(26); UK CRR Art. 4(1)(26).
[35] *See* Basel Framework CRE20.42. For example, corporate exposures rated AAA to AA− are assigned a 20% risk weight, and those rated A+ to A− are assigned a 50% risk weight. The EU CRR and the UK CRR follow the Basel Framework approach. *See* EU CRR Art. 122; UK CRR Art. 122.

whose parent has, publicly traded securities outstanding should qualify for a 65% risk weight under the ERB Approach.

However, this would leave out many creditworthy and well capitalized insurance companies, who would remain subject to the 100% risk weight. In Question 39 of the Proposal, the Agencies pose the following questions:

> For what reasons, if any, should the agencies consider applying a lower risk weight than 100 percent to exposures to companies that are not publicly traded ***but are companies that are "highly regulated?"*** What, if any, criteria should the agencies consider to identify companies that are "highly regulated?" Alternatively, ***what are the advantages and disadvantages of assigning lower risk weights to highly regulated entities*** (such as open-ended mutual funds, mutual insurance companies, pension funds, or registered investment companies)?[36]

The Agencies clearly recognize that there may be compelling arguments for distinguishing between general non-publicly traded companies and those that are "highly regulated." As we discuss in more detail below, we believe that exposures to prudentially regulated insurance companies should be afforded a lower risk weight under the U.S. Basel III Regulations comparable to other highly regulated financial institutions.

For example, following the Basel Framework's approach for exposures to banks in jurisdictions that do not allow the use of external ratings for regulatory purposes, the Agencies have proposed to assign a risk weight generally between 40% and 150% for bank exposures, depending on the bank's creditworthiness.

- ***Grade A bank exposures*** would receive a 40% risk weight. These are bank exposures for which the obligor depository institution, foreign bank or credit union (i) is investment grade and (ii) whose most recent publicly disclosed capital ratios meet or exceed the higher of: (a) the minimum capital requirements and any additional amounts necessary to not be subject to limitations on distributions and discretionary bonus payments under the capital rules established by the prudential supervisor of the depository institution, foreign bank, or credit union, and (b) if applicable, the capital ratio requirements for the well-capitalized category under the Agencies' prompt corrective action framework (or under similar rules of the National Credit Union Administration).
- ***Grade B bank exposures*** would receive a 75% risk weight. These are bank exposures that are not Grade A bank exposures and for which the obligor depository institution, foreign bank, or credit union (1) is speculative grade or investment grade, and (2) whose most recent publicly disclosed capital ratios meet or exceed the higher of: (a) the applicable minimum capital requirements under capital rules established by the prudential supervisor of the depository institution, foreign bank, or credit union, and (b) if applicable, the capital ratio requirements for the adequately-capitalized category under the Agencies' prompt

[36] Proposal, *supra* note 1, at 64054 (emphasis added).

corrective action framework (or under similar rules of the National Credit Union Administration).

- ***Grade C bank exposures*** would receive a 150% risk weight. These are bank exposures that do not qualify as a Grade A or Grade B bank exposure.

Exposures to insurance companies are, in our view, more analogous to exposures to Grade A or Grade B banks than to other types of corporate entities (whether or not publicly traded). This is because U.S. insurance companies are subject to extensive prudential regulation and oversight from state insurance regulators, and foreign insurance companies in certain jurisdictions are subject to similar regulation from their insurance regulators.

Thus, RAA respectfully suggests the Agencies add a new requirement that pursuant to the new expanded risk-based approach banking organizations must assign a risk weight to an exposure covered by an eligible guarantee provided by a qualifying insurance company as follows:

Category of qualifying insurance company exposure	Grade A qualifying insurance company exposure	Grade B qualifying insurance company exposure	Grade C qualifying insurance company exposure
Base risk weight	40%	75%	150%
Risk weight for a qualifying insurance company exposure that is a self-liquidating, trade-related contingent item that arises from the movement of goods and has a maturity of three months or less	20%	50%	150%

We propose to generally align the approach for Grade A, B and C qualifying insurance company exposures with that taken by the Agencies for Grade A, B and C bank exposures under the Proposal.

- ***Grade A qualifying insurance company exposure*** would mean the portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company that is (i) investment grade and (ii) exceeds the minimum risk-based capital, solvency capital or similar requirements established by its State insurance regulator or foreign insurance regulator by an amount at least equal to the additional buffer percentage[37] of the applicable minimum.

[37] For purposes of this definition, the *additional buffer percentage* would be an amount (expressed as a percentage) equal to the 2.5 percent minimum capital conservation buffer at or below which a banking organization is subject to limits on distributions and discretionary bonus payments under the current U.S. Basel III Regulations *divided by* the 4.5 percent minimum common equity tier 1 capital ratio under the current U.S. Basel III Regulations.

- ***Grade B qualifying insurance company exposure*** would mean the portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company that (i) is not a Grade A qualifying insurance company exposure, (ii) is speculative grade or investment grade and (iii) meets or exceeds the minimum risk-based capital, solvency capital or similar requirements established by its State insurance regulator or foreign insurance regulator.

Notwithstanding the above definitions, an exposure would not be treated as a Grade A or Grade B qualifying insurance company exposure, as applicable, if (i) data concerning the relevant insurance company's compliance with the minimum risk-based capital, solvency capital or similar requirements established by its State insurance regulator have not been publicly disclosed within the previous 12 months, (ii) the relevant insurance company's external auditor has issued an adverse audit opinion or has expressed substantial doubt about the ability of the qualifying insurance company to continue as a going concern within the previous 12 months, or (iii) with respect to a foreign insurance company, the foreign insurance company is not domiciled and licensed in a foreign country that (A) is (or is a member state of) a jurisdiction subject to a covered agreement or (B) is a reciprocal jurisdiction.

- ***Grade C qualifying insurance company exposure*** means the portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company that does not qualify as a Grade A or Grade B qualifying insurance company exposure.

The full text of our proposal is attached as Appendix A, and a related explanatory document is attached as Appendix B.

CONCLUSION

Thank you for the opportunity to provide comments. The RAA and its members would be happy to follow up with you regarding the recommendations in this letter or answer any questions you may have.

Sincerely,

J. Lee Covington II
President

APPENDIX A

Proposed Amendments to the US Basel III Implementing Regulations

---

Subpart A—General Provisions

§ ___.2 Definitions.

* * *

Covered agreement means a covered agreement as defined in section 502 of the Dodd-Frank Act (31 U.S.C. 313(r)(2)).

* * *

Eligible guarantee means a guarantee that:

* * *

(2) Is either:

(i) Unconditional (*i.e.*, includes no provision outside the direct control of the beneficiary, the non-satisfaction of which would give the protection provider the contractual right to refuse payment under the guarantee), or

(ii) A contingent obligation of the U.S. government or its agencies, the enforceability of which is dependent upon some affirmative action on the part of the beneficiary of the guarantee or a third party (for example, meeting servicing requirements);

* * *

Eligible guarantor means:

A sovereign, the Bank for International Settlements, the International Monetary Fund, the European Central Bank, the European Commission, a Federal Home Loan Bank, Federal Agricultural Mortgage Corporation (Farmer Mac), the European Stability Mechanism, the European Financial Stability Facility, a multilateral development bank (MDB), a depository institution, a bank holding company, a savings and loan holding company, a credit union, a foreign bank, ~~or~~ a qualifying central counterparty, or a qualifying insurance company; or

(2) An entity (other than a special purpose entity):

(i) That at the time the guarantee is issued or anytime thereafter, has issued and outstanding an unsecured debt security without credit enhancement that is investment grade;

(ii) Whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees; and

(iii) That is not an insurance company engaged predominately in the business of providing credit protection (such as a monoline bond insurer or re-insurer).

* * *

Foreign insurance company means any entity that is:

(1) organized under the laws of a foreign country;

(2) engaged in the business of insurance;

(3) supervised and regulated by a foreign insurance regulator in a manner similar to a U.S. insurance company; and

(4) covered by a law of the foreign country that is designed to specifically deal with the rehabilitation, liquidation, or insolvency of an insurance company.

* * *

Grade A qualifying insurance company exposure means:

(1) The portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company (to the extent that the eligible guarantee meets the requirements of § ___.120) for which the qualifying insurance company is investment grade and exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator or foreign insurance regulator by an amount at least equal to the additional buffer percentage of the applicable minimum.

(2) For purposes of paragraph (1) of this definition, *additional buffer percentage* means an amount, expressed as a percentage, equal to:

(A) the minimum capital conservation buffer at or below which a [BANKING ORGANIZATION] is subject to limits on distributions and discretionary bonus payments under § ___.11(a)(4); divided by

(B) the minimum common equity tier 1 capital ratio under § ___.10.

(3) Notwithstanding paragraph (1) of this definition, an exposure is not a Grade A qualifying insurance company exposure if:

(A) Data concerning the qualifying insurance company's compliance with the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator or foreign insurance regulator have not been publicly disclosed within the previous 12 months;

(B) The qualifying insurance company's external auditor has issued an adverse audit opinion or has expressed substantial doubt about the ability of the qualifying insurance company to continue as a going concern within the previous 12 months; or

(C) For a foreign insurance company, the foreign insurance company is not domiciled and licensed in a foreign country that:

(i) is (or is a member state of) a jurisdiction subject to a covered agreement, or

(ii) is a reciprocal jurisdiction.

Grade B qualifying insurance company exposure means:

(1) The portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company (to the extent that the eligible guarantee meets the requirements of § ___.120) that is not a Grade A qualifying insurance company exposure and for which the qualifying insurance company is speculative grade or investment grade and meets or exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator or foreign insurance regulator.

(2) Notwithstanding paragraph (1) of this definition, an exposure is not a Grade B qualifying insurance company exposure if:

(A) Data concerning the qualifying insurance company's compliance with the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator or foreign insurance regulator have not been publicly disclosed within the previous 12 months;

(B) The qualifying insurance company's external auditor has issued an adverse audit opinion or has expressed substantial doubt about the ability of the qualifying insurance company to continue as a going concern within the previous 12 months; or

(C) For a foreign insurance company, the foreign insurance company is not domiciled and licensed in a foreign country that:

(i) is (or is a member state of) a jurisdiction subject to a covered agreement, or

(ii) is a reciprocal jurisdiction.

Grade C qualifying insurance company exposure means the portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company (to the extent that the eligible guarantee meets the requirements of § ___.120) that does not qualify as a Grade A qualifying insurance company exposure or a Grade B qualifying insurance company exposure.

*   *   *

Qualifying insurance company means, with respect to any guarantee, a U.S. insurance company or foreign insurance company:

(1) That at the time the guarantee is issued or anytime thereafter,

(A) has (or is controlled by a company that has) issued and outstanding an unsecured debt security without credit enhancement that is investment grade, or

(B) is investment grade and has (or is controlled by a company that has) a publicly traded security outstanding;

(2) That, in the case of a U.S. insurance company, meets or exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator;

(3) That, in the case of a foreign insurance company:

(A) is domiciled and licensed in a foreign country that:

(i) is (or is a member state of) a jurisdiction subject to a covered agreement, or

(ii) is a reciprocal jurisdiction; and

(B) meets or exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its foreign insurance regulator;

(4) Whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees or, if its creditworthiness is positively correlated with the credit risk of the exposures for which it has provided guarantees, that has demonstrated to the satisfaction of the [BANKING ORGANIZATION], in accordance with the [BANKING ORGANIZATION]'s capital and credit-risk management policies and procedures, either:

(A) that it has mitigated the associated risk, or

(B) that it has a diversified concentration risk profile; and

(5) That is not an insurance company engaged predominately in the business of providing credit protection (such as a monoline bond insurer or re-insurer) or, if its creditworthiness is positively correlated with the credit risk of the exposures for which it has provided guarantees, that has demonstrated to the satisfaction of the [BANKING ORGANIZATION], in accordance with the [BANKING ORGANIZATION]'s capital and credit-risk management policies and procedures, either:

(A) that it has mitigated the associated risk, or

(B) that it has a diversified concentration risk profile.

* * *

Reciprocal jurisdiction means a non-U.S. jurisdiction that is included on the National Association of Insurance Commissioners (NAIC) List of Reciprocal Jurisdictions pursuant to the NAIC Credit for Reinsurance Model Law and Regulation.

* * *

Subpart E—Risk-Weighted Assets—Expanded Risk-Based Approach

§ ___.111 General Risk Weights.

* * *

(_) *Certain exposures to qualifying insurance companies.*

(1) A [BANKING ORGANIZATION] must assign a risk weight to the portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company (to the extent that the eligible guarantee meets the requirements of § ___.120) in accordance with Table • of this section, unless otherwise provided under paragraph (_)(2) of this section.

TABLE • TO § ___.111—CERTAIN QUALIFYING INSURANCE COMPANY EXPOSURES

Category of qualifying insurance company exposure	Grade A qualifying insurance company exposure	Grade B qualifying insurance company exposure	Grade C qualifying insurance company exposure
Base risk weight	40%	75%	150%

Risk weight for a qualifying insurance company exposure that is a self-liquidating, trade-related contingent item that arises from the movement of goods and has a maturity of three months or less	20%	50%	150%

(2) Notwithstanding paragraph (_)(1) of this section, a [BANKING ORGANIZATION] must not assign a risk weight to a foreign insurance company exposure lower than the risk weight applicable to a sovereign exposure of the home country of the foreign insurance company unless:

(A) The exposure is in the local currency of the home country of the foreign insurance company;

(B) For an exposure to a branch of the foreign insurance company in a foreign jurisdiction that is not the home country of the foreign insurance company, the exposure is in the local currency of the jurisdiction in which the foreign branch operates; or

(C) The exposure is a self-liquidating, trade-related contingent item that arises from the movement of goods and that has a maturity of three months or less.

APPENDIX B

Explanation of the RAA's Proposed Amendments to
12 CFR Parts 3, 217 and 324 (the "**U.S. Basel III Regulations**")

A. Definition of "eligible guarantee"

Clause (2) of the definition of "eligible guarantee" in § __.2 of the U.S. Basel III Regulations adopted by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation (the "**Agencies**") in July 2013 (the "**2013 Regulations**")[1] provides that eligible guarantees (other than certain contingent obligations of the U.S. government or its agencies) must be "unconditional." The Agencies have not provided published guidance addressing whether this requirement applies to *all* conditions to the protection provider's performance (including, for example, payment of premiums and beneficiary reporting obligations) or only conditions outside the direct control of the beneficiary (for example, a "nuclear" coverage exclusion). The Agencies' July 2023 regulatory capital proposal for large banking organizations (the "**Endgame Proposal**")[2] would not modify the 2013 Regulations' "eligible guarantee" definition.

Provisions of the standards adopted by Basel Committee on Banking Supervision (the "**Basel Framework**") that deal with credit risk mitigation under the standardized approach set forth operational requirements for guarantees and credit derivatives, including a requirement that a guarantee or credit derivative "must be unconditional; there should be no clause in the protection contract *outside the direct control of the bank* that could prevent the protection provider from being obliged to pay out in a timely manner in the event that the underlying counterparty fails to make the payment(s) due."[3] Following the Basel Framework's approach, the credit risk mitigation provisions of the EU Capital Requirements Regulation (the "**EU CRR**") provide that credit protection deriving from a guarantee or credit derivative shall qualify as eligible unfunded credit protection only if "the credit protection contract does not contain any clause, the fulfilment of which is *outside the direct control of the lender*, that [among other things] could prevent the protection provider from being obliged to pay out in a timely manner in the event that the original obligor fails to make any payments due."[4] The UK "onshored" Capital Requirements Regulation (the "**UK CRR**") contains identical language.[5]

---

[1] Office of the Comptroller of the Currency and Board of Governors of the Federal Reserve System, *Final Rule*, 78 Fed. Reg. 62018 (Oct. 11, 2013); Federal Deposit Insurance Corporation, *Interim Final Rule*, 78 Fed. Reg. 55340 (Sept. 10, 2013).

[2] Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System and Federal Deposit Insurance Corporation, *Notice of Proposed Rulemaking*, 88 Fed. Reg. 64028 (Sept. 18, 2023).

[3] Basel Framework CRE22.71(5) (emphasis added).

[4] EU CRR Art. 213(1)(c) (emphasis added).

[5] *See* UK CRR Art. 213(1)(c).

In light of the above, the RAA proposes that clause (2)(i) of the definition of "eligible guarantee" in § __.2 of the 2013 Regulations be amended to add, after the word "unconditional," the parenthetical phrase "(*i.e.*, includes no provision outside the direct control of the beneficiary, the non-satisfaction of which would give the protection provider the contractual right to refuse payment under the guarantee)."

B. Definition of "eligible guarantor"

1. Specifically eligible guarantors

Clause (1) of the definition of "eligible guarantor" in § __.2 of the 2013 Regulations, which is unchanged in the Endgame Proposal, lists "[a] sovereign, the Bank for International Settlements, the International Monetary Fund, the European Central Bank, the European Commission, a Federal Home Loan Bank, Federal Agricultural Mortgage Corporation (Farmer Mac), the European Stability Mechanism, the European Financial Stability Facility, a multilateral development bank (MDB), a depository institution, a bank holding company, a savings and loan holding company, a credit union, a foreign bank, or a qualifying central counterparty" as specifically eligible guarantors. The list does not include an insurance company.

The standardized approach credit risk mitigation provisions of the Basel Framework, describing the entities, credit protection given by which can be recognized, lists "[s]overeign entities, PSEs, multilateral development banks (MDBs), banks, securities firms and other prudentially regulated financial institutions with a lower risk weight than the counterparty" as specifically eligible guarantors.[6] The relevant provision goes on to state that—

> "A prudentially regulated financial institution is defined as: a legal entity supervised by a regulator that imposes prudential requirements consistent with international norms or a legal entity (parent company or subsidiary) included in a consolidated group where any substantial legal entity in the consolidated group is supervised by a regulator that imposes prudential requirements consistent with international norms. These include, but are not limited to, *prudentially regulated insurance companies*, broker/dealers, thrifts and futures commission merchants, and qualifying central counterparties as defined in CRE54."[7]

Note that neither the EU CRR nor the UK CRR includes insurance companies (prudentially regulated or otherwise) in its list of specifically eligible guarantors.[8]

[6] Basel Framework CRE22.76(1).

[7] Basel Framework CRE22.76(1), fn. 11 (emphasis added).

[8] *See* EU CRR Art. 201(1); UK CRR Art. 201(1).

However, following the Basel Framework's approach for other eligible guarantors "[i]n jurisdictions that allow the use of external ratings for regulatory purposes,"[9] both the EU CRR and the UK CRR include corporate entities that have a credit assessment by an "eligible credit assessment institution" as eligible guarantors.[10] It would be reasonable to assume that many externally rated insurance companies qualify as eligible guarantors for purposes of the EU CRR and the UK CRR on this basis.

Section 939A of the Dodd-Frank Act, of course, required the Agencies to remove all references to external ratings from their regulations, including capital adequacy requirements, and the U.S. Basel III Regulations accordingly do not take external ratings into account in defining who may be deemed an eligible guarantor. Therefore, reflecting the Basel Framework's inclusion of prudentially regulated insurance companies in its list of specifically eligible guarantors, the RAA proposes that a "qualifying insurance company" be added to the list of specifically eligible guarantors in clause (1) of the definition of "eligible guarantor" in § __.2 of the 2013 Regulations.[11]

2. Other eligible guarantors

Clause (2) of the definition of "eligible guarantor" in § __.2 of the 2013 Regulations, which is unchanged in the Endgame Proposal, sets forth the criteria for eligible guarantors other than the specifically eligible guarantors listed in clause (1) of the definition:

> An entity (other than a special purpose entity):
>
> (i) That at the time the guarantee is issued or anytime thereafter, has issued and outstanding an unsecured debt security without credit enhancement that is investment grade;
>
> (ii) Whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees; and
>
> (iii) That is not an insurance company engaged predominately in the business of providing credit protection (such as a monoline bond insurer or re-insurer).

Clauses (2)(i), (2)(ii) and (2)(iii) above are referred to as the "**Outstanding Investment Grade Debt Requirement**," the "**No Positive Correlation Requirement**" and the "**Monoline Exclusion**," respectively, for purposes of this memorandum.

---

[9] Basel Framework CRE22.76(2).

[10] *See* EU CRR Art. 201(1)(g)(1); UK CRR Art. 201(1)(g)(1); *see also* Basel Framework CRE22.76(2) (jurisdictions that allow the use of external ratings for regulatory purposes).

[11] *See* "'Qualifying insurance company'—RAA's proposed definition" below.

By way of comparison, the Basel Framework's approach for other eligible guarantors "[i]n jurisdictions that do not allow the use of external ratings for regulatory purposes"[12] recognizes credit protection given by—

> Other entities, defined as "investment grade" meaning they have adequate capacity to meet their financial commitments (including repayments of principal and interest) in a timely manner, irrespective of the economic cycle and business conditions. When making this determination, the bank should assess the entity against the investment grade definition taking into account the complexity of its business model, performance against industry and peers, and risks posed by the entity's operating environment. Moreover, the following conditions will have to be met:
>
> (i) For corporate entities (or the entity's parent company), they must have securities outstanding on a recognised securities exchange;
>
> (ii) The creditworthiness of these "investment grade entities" is not positively correlated with the credit risk of the exposures for which they provided guarantees.[13]

As explained below, the Basel Framework's approach differs in key respects from clause (2) of the definition of "eligible guarantor" in the 2013 Regulations.

a. Outstanding Investment Grade Debt Requirement

The requirement in the Basel Framework that an eligible guarantor "have securities outstanding on a recognised securities exchange"—which parallels (and serves essentially the same purposes as) the Outstanding Investment Grade Debt Requirement—permits consideration of securities issued by the eligible guarantor's parent company as well as those issued by the eligible guarantor itself. The Basel Framework's approach recognizes that insurance companies typically do not issue debt securities, investment grade, exchange traded or otherwise; instead, debt issuance and similar financing functions are performed by the insurance companies' parent holding companies.

b. No Positive Correlation Requirement

Although the language of the No Positive Correlation Requirement and the nearly identical Basel Framework provision is not entirely clear, both provisions appear to be aimed at exposures to guarantors that exhibit "wrong-way risk," as defined in the 2013 Regulations.[14] As such, the No

---

[12] Basel Framework CRE22.76(3).

[13] Basel Framework CRE22.76(3)(a). Note that, because the European Union and the United Kingdom *do* allow the use of external ratings for regulatory purposes, the EU CRR and the UK CRR do not contain analogous provisions. *See* note 10, *supra*, and accompanying text.

[14] The 2013 Regulations define "wrong-way risk" as "the risk that arises when an exposure to a particular counterparty is positively correlated with the probability of default of such counterparty itself." 12 CFR 3.2, 217.2, 324.2.

Positive Correlation Requirement effectively, and by its terms, requires *zero* positive correlation between an exposure to an eligible guarantor and the probability of the guarantor's default. Whether zero positive correlation is statistically achievable in actual practice is open to question. Moreover, the No Positive Correlation Requirement does not account for measures by guarantors to mitigate the risks associated with positive correlation, nor does it take into consideration whether guarantors exhibiting non-zero positive correlation nevertheless have a diversified concentration risk profile.

c. Monoline Exclusion

The Basel Framework does not contain any provision similar to the Monoline Exclusion in the 2013 Regulations' definition of "eligible guarantor." Because both the Monoline Exclusion and the No Positive Correlation Requirement arise from policy concerns about wrong-way risk, it seems fair to assume that the drafters of the Basel Framework thought a provision similar to the Monoline Exclusion would be duplicative.

C. "Qualifying insurance company"

1. RAA's proposed definition

The RAA's proposed amendments to the 2013 Regulations would define "qualifying insurance company" (also referred to herein as a "**QIC**") as follows:

> *Qualifying insurance company* means, with respect to any guarantee, a U.S. insurance company or foreign insurance company:
>
> (1) That at the time the guarantee is issued or anytime thereafter,
>
> (A) has (or is controlled by a company that has) issued and outstanding an unsecured debt security without credit enhancement that is investment grade, or
>
> (B) is investment grade and has (or is controlled by a company that has) a publicly traded security outstanding;
>
> (2) That, in the case of a U.S. insurance company, meets or exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator;
>
> (3) That, in the case of a foreign insurance company:
>
> (A) is domiciled and licensed in a foreign country that:
>
> (i) is (or is a member state of) a jurisdiction subject to a covered agreement, or
>
> (ii) is a reciprocal jurisdiction; and
>
> (B) meets or exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its foreign insurance regulator;

> (4) Whose creditworthiness is not positively correlated with the credit risk of the exposures for which it has provided guarantees or, if its creditworthiness is positively correlated with the credit risk of the exposures for which it has provided guarantees, that has demonstrated to the satisfaction of the [BANKING ORGANIZATION], in accordance with the [BANKING ORGANIZATION]'s capital and credit-risk management policies and procedures, either:
>
> (A) that it has mitigated the associated risk, or
>
> (B) that it has a diversified concentration risk profile; and
>
> (5) That is not an insurance company engaged predominately in the business of providing credit protection (such as a monoline bond insurer or re-insurer) or, if its creditworthiness is positively correlated with the credit risk of the exposures for which it has provided guarantees, that has demonstrated to the satisfaction of the [BANKING ORGANIZATION], in accordance with the [BANKING ORGANIZATION]'s capital and credit-risk management policies and procedures, either:
>
> (A) that it has mitigated the associated risk, or
>
> (B) that it has a diversified concentration risk profile.

Clauses (1), (4) and (5) of the RAA's proposed "qualifying insurance company" definition correspond to the Outstanding Investment Grade Debt Requirement, the No Positive Correlation Requirement and the Monoline Exclusion (clauses (2)(i), (2)(ii) and (2)(iii) of the definition of "eligible guarantor" in § __.2 of the 2013 Regulations), with certain modifications described below. Clauses (2) and (3) of the proposed "qualifying insurance company" definition set forth additional requirements related to the prudential regulation of QICs.

2. Prudential regulation of QICs

a. U.S. insurance companies

In the case of a U.S. insurance company, clause (2) of the RAA's proposed "qualifying insurance company" definition would require that the insurance company meet or exceed the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator.

b. Foreign insurance companies

In the case of a foreign insurance company, clause (3) of the RAA's proposed "qualifying insurance company" definition would require that the insurance company meet or exceed the minimum risk-based capital, solvency capital, or similar requirements established by its foreign insurance regulator *and* that it be domiciled and licensed in a foreign country that satisfies one or both of the conditions described below.

First, the foreign country is (or is a member state of) a jurisdiction subject to a "covered agreement" under Section 502 of the Dodd-Frank Act, which created the Federal Insurance Office. Section 502 provides:

> The term "covered agreement" means a written bilateral or multilateral agreement regarding prudential measures with respect to the business of insurance or reinsurance that—
>
> (A) is entered into between the United States and one or more foreign governments, authorities, or regulatory entities; and
>
> (B) relates to the recognition of prudential measures with respect to the business of insurance or reinsurance that achieves a level of protection for insurance or reinsurance consumers that is substantially equivalent to the level of protection achieved under State insurance or reinsurance regulation.[15]

Currently, the United States has Dodd-Frank Act covered agreements in effect with the European Union and the United Kingdom.

Second, the foreign country is a "reciprocal jurisdiction" included on the National Association of Insurance Commissioners (the "**NAIC**") List of Reciprocal Jurisdictions pursuant to the NAIC Credit for Reinsurance Model Law and Regulation. The NAIC has stated that—

> The standard for qualification of a jurisdiction is that the NAIC must reasonably conclude that the jurisdiction's reinsurance supervisory system achieves a level of effectiveness in financial solvency regulation that is deemed acceptable for purposes of reinsurance collateral reduction, that the jurisdiction's demonstrated practices and procedures with respect to reinsurance supervision are consistent with its reinsurance supervisory system, and that the jurisdiction's laws and practices satisfy the criteria required of Qualified Jurisdictions as set forth in the Credit for Reinsurance Models.[16]

Currently, the NAIC reciprocal jurisdictions include all European Union member states and the United Kingdom pursuant to Dodd-Frank Act covered agreements, plus Bermuda,[17] Japan, and Switzerland.

c. Definition of "foreign insurance company"

For purposes of the "qualifying insurance company" definition, the RAA also proposes to add to § __.2 of the 2013 Regulations the following defined term:

---

[15] 31 USC 313(r)(2).

[16] NAIC, *Process for Evaluating Qualified and Reciprocal Jurisdictions*, at 9 (Aug. 17, 2021).

[17] Bermuda's status as an NAIC reciprocal jurisdiction is currently applicable only to (re)insurers of Class 3A, Class 3B and Class 4, and long-term insurers of Class C, Class D and Class E.

> *Foreign insurance company* means any entity that is:
>
> (1) organized under the laws of a foreign country;
>
> (2) engaged in the business of insurance;
>
> (3) supervised and regulated by a foreign insurance regulator in a manner similar to a U.S. insurance company; and
>
> (4) covered by a law of the foreign country that is designed to specifically deal with the rehabilitation, liquidation, or insolvency of an insurance company.

The 2013 Regulations do not define "foreign insurance company" (the definition of "insurance company" in the 2013 Regulations refers to the Dodd-Frank Act definition, which is limited to U.S. insurance companies).

3. Other criteria for QICs

a. Outstanding Investment Grade Debt Requirement for QICs

Clause (1) of the RAA's proposed definition of "qualifying insurance company" would modify the Outstanding Investment Grade Debt Requirement (as it applies to QICs) to permit consideration of securities issued by a parent holding company that controls the QIC, as well as those issued by the QIC itself.[18] Similar to the Basel Framework's approach, the modified Outstanding Investment Grade Debt Requirement would recognize that insurance companies typically do not issue debt securities and that debt issuance and similar financing functions are performed by the insurance companies' parent holding companies.[19] Additionally, in the case of a QIC that does not satisfy the modified Outstanding Investment Grade Debt Requirement, clause (1) of the proposed definition would allow "qualifying insurance company" status if the QIC is investment grade and has (or is controlled by a parent holding company that has) publicly traded securities outstanding.[20]

b. No Positive Correlation Requirement for QICs

Clause (4) of the RAA's proposed "qualifying insurance company" definition would modify the No Positive Correlation Requirement (as it applies to QICs). Although continuing generally to require zero positive correlation between an exposure to a QIC and the probability of

---

[18] The U.S. Basel III Regulations provide that a company "controls" another company if the first company (i) owns, controls, or holds with power to vote 25% or more of a class of voting securities of the second company or (ii) consolidates the second company for financial reporting purposes. *See* 12 CFR 3.2, 217.2, 324.2.

[19] *See* "Definition of 'eligible guarantor'—Other eligible guarantors—Outstanding Investment Grade Debt Requirement" above.

[20] The U.S. Basel III Regulations provide that securities are "publicly traded" if they are traded on (i) any exchange registered as a national securities exchange under the Securities Exchange Act of 1934 or (ii) any non-U.S. securities exchange that is authorized by a national securities regulatory authority and provides a liquid, two-way market for such securities. *See* 12 CFR 3.2, 217.2, 324.2.

the QIC's default, clause (4) would permit non-zero positive correlation if the QIC demonstrates to the satisfaction of the banking organization, in accordance with the banking organization's capital and credit risk management policies and procedures, either (A) that the QIC has mitigated the associated risk (for example, through reinsurance arrangements or other eligible guarantees); or (B) that the QIC has a diversified concentration risk profile.[21] The modified No Positive Correlation Requirement would provide banking organizations with a choice of practical approaches to the management of wrong-way risk in the insurance context.[22]

c. Monoline Exclusion for QICs

Clause (5) of the RAA's proposed "qualifying insurance company" definition would also modify the Monoline Exclusion (as it applies to QICs). The general exclusion of insurance companies engaged predominately in the business of providing credit protection (such as monoline bond insurers and re-insurers) would be left in place, but—to the extent that such an insurance company exhibits non-zero positive correlation—clause (5) would permit the insurance company to be a "qualifying insurance company" if it demonstrates to the satisfaction of the banking organization, in accordance with the banking organization's capital and credit risk management policies and procedures, either (A) that the insurance company has mitigated the associated risk (for example, through reinsurance arrangements or other eligible guarantees); or (B) that the insurance company has a diversified concentration risk profile.[23]

D. Risk-weighting of exposures to QICs

1. Risk weights under the "expanded risk-based approach"

a. Exposures to corporates

Exposures to insurance companies are treated as corporate exposures under the standardized approach in both the U.S. Basel III Regulations and the Basel Framework, as well as under the EU CRR and the UK CRR.[24] Under the Basel Framework, exposures to "rated"

[21] Generally speaking, a banking organization's or a counterparty's "concentration risk profile" is a snapshot of its overall credit exposure concentrations with respect to single counterparties, affiliated groups, industry sectors, collateral types and geographic regions at any given time. *See* FDIC Office of Inspector General, *Forward-Looking Supervision* 7 n.11 (Evaluation Report 18-004, August 2018). A "diversified" concentration risk profile has fewer and/or smaller concentrations of credit exposure than a concentration risk profile that is relatively undiversified.

[22] *See* "Definition of 'eligible guarantor'—Other eligible guarantors—No Positive Correlation Requirement" above.

[23] *See* "Definition of 'eligible guarantor'—Other eligible guarantors—Monoline Exclusion" above.

[24] The Basel Framework, the EU CRR and the UK CRR all contemplate exposures to "financial institutions" subject to certain prudential requirements being treated as exposures to banks for risk-weighting purposes. *See* Basel Framework CRE20.40; EU CRR Art. 119(5); UK CRR Art. 119(5). However, none of the three regimes define the term "financial institution" to include insurance companies. *See* Basel Framework SCO30.1; EU CRR Art. 4(1)(26); UK CRR Art. 4(1)(26).

corporates "in jurisdictions that allow the use of external ratings for regulatory purposes" are assigned risk weights ranging from 20% to 150% in accordance with their "eligible credit assessment institution" ratings.[25] In the case of exposures to corporates "in jurisdictions that do not allow the use of external ratings for regulatory purposes," the Basel Framework assigns a 100% risk weight, with the exception of "investment grade" corporate exposures, which may be assigned a 65% risk weight.[26]

Under the standardized approach in the 2013 Regulations, all exposures to corporates are assigned a 100% risk weight. No exception is made for investment grade corporate exposures, notwithstanding the Basel Framework. However, the Endgame Proposal's "expanded risk-based approach" (the "**ERBA**") for large banking organizations follows the Basel Framework and assigns a 65% risk weight to "a corporate exposure that is an exposure to a company that is investment grade and that has a publicly traded security outstanding or that is controlled by a company that has a publicly traded security outstanding."[27] For purposes of the U.S. Basel III Regulations, a company is "investment grade" if it—

> has adequate capacity to meet financial commitments for the projected life of the asset or exposure. Such an entity or reference entity has adequate capacity to meet financial commitments if the risk of its default is low and the full and timely repayment of principal and interest is expected.[28]

It is reasonable to expect that exposures to many, if not most, U.S. and foreign insurance companies that have (or are controlled by parent holding companies that have) publicly traded securities outstanding would be assigned a 65% risk weight under the ERBA.[29]

---

[25] *See* Basel Framework CRE20.42. For example, corporate exposures rated AAA to AA− are assigned a 20% risk weight, and those rated A+ to A− are assigned a 50% risk weight. The EU CRR and the UK CRR follow the Basel Framework approach. *See* EU CRR Art. 122; UK CRR Art. 122.

[26] *See* Basel Framework CRE20.44, 20.46. Because the European Union and the United Kingdom *do* allow the use of external ratings for regulatory purposes, the EU CRR and the UK CRR do not contain analogous provisions.

[27] Endgame Proposal, 88 Fed. Reg. at 64192 (§ __.111(h) of the proposed common rule). *See* note 18 (definition of "control") and note 20 (definition of "publicly traded"), *supra*.

[28] 12 CFR 3.2, 217.2, 324.2; *see* Endgame Proposal, 88 Fed. Reg. at 64054 ("A banking organization's investment grade analysis is dependent upon the banking organization's underwriting criteria, judgment, and assumptions.").

[29] In its discussion of "investment grade" corporate exposures, the Endgame Proposal requested comment on the following question:

> "For what reasons, if any, should the agencies consider applying a lower risk weight than 100 percent to exposures to companies that are not publicly traded but are companies that are 'highly regulated?' What, if any, criteria should the agencies consider to identify companies that are 'highly regulated?' Alternatively, what are the advantages and disadvantages of assigning lower risk weights to highly regulated entities (such as open-ended mutual funds, mutual insurance companies, pension funds, or registered investment companies)?"

Endgame Proposal, 88 Fed. Reg. at 64054 (Question 39). This question appears to be directed mainly at companies unable to satisfy the outstanding publicly traded securities requirement for the new 65% risk weight that would apply

b. Exposures to banks

Under the Endgame Proposal's ERBA, exposures to banks (defined to include exposures to U.S. depository institutions, foreign banks and credit unions) are categorized as "Grade A," "Grade B" or "Grade C" depending on whether the bank is "investment grade" or "speculative grade" and whether the bank's capital ratios meet or exceed certain thresholds.[30] A bank exposure is Grade A if, among other things, the bank is investment grade and its most recent capital ratios meet or exceed the minimum capital requirements and "any additional amounts [*i.e.*, buffers] necessary to not be subject to limitations on distributions and discretionary bonus payments under capital rules established by the [bank's] prudential supervisor."[31] A bank exposure that does not qualify as Grade A is Grade B if, among other things, the bank is speculative grade or investment grade and its most recent capital ratios meet or exceed the minimum capital requirements under capital rules established by the bank's prudential supervisor. A bank exposure that does not qualify as either Grade A or Grade B is a Grade C bank exposure.

Grade A, Grade B and Grade C bank exposures would be assigned risk weights of 40%, 75% and 150%, respectively, subject to a floor, in the case of a foreign bank, equal to the risk weight assigned to sovereign exposures of the foreign bank's home country.[32] The treatment of bank exposures under the ERBA generally aligns with the Basel Framework's Standardised Credit Risk Assessment Approach (the "**SCRA**") for exposures to banks in jurisdictions that do not allow the use of external ratings for regulatory purposes.[33]

---

to "investment grade" corporate exposures. But the Agencies' interest in exposures to "highly regulated" companies suggests the possibility that prudentially regulated insurance companies (*i.e.*, QICs) could, under the ERBA, be treated more like banks. *See* "Risk-weighting of exposures to QICs—RAA's proposed treatment of exposures to QICs under the ERBA" below.

[30] Endgame Proposal, 88 Fed. Reg. at 64184-64185 (§ __.101(b) of the proposed common rule). For purposes of the U.S. Basel III Regulations, a bank is "speculative grade" if it "has adequate capacity to meet financial commitments in the near term, but is vulnerable to adverse economic conditions, such that should economic conditions deteriorate, the [bank] would present an elevated default risk." 12 CFR 3.2, 217.2, 324.2. *See also* note 28, *supra* (definition of "investment grade").

[31] Endgame Proposal, 88 Fed. Reg. at 64184-64185 (§ __.101(b) of the proposed common rule). In the case of a U.S. banking organization, the applicable buffer is the capital conservation buffer, below which the banking organization is subject to limits on distributions and discretionary bonus payments under the U.S. Basel III Regulations. *See* 12 CFR 3.11(a)(4), 217.11(a)(4), 324.11(a)(4).

[32] Endgame Proposal, 88 Fed. Reg. at 64188-64189 (§ __.111(d) of the proposed common rule). Grade A and Grade B bank exposures that are self-liquidating, trade-related contingent items that arise from the movement of goods and that have a maturity of three months or less would be assigned risk weights of 20% and 50%, respectively.

[33] *See* Basel Framework CRE20.21-20.32. Under the SCRA, for a bank exposure to be classified as Grade A and assigned a 40% risk weight, the bank "must meet or exceed the published minimum regulatory requirements *and buffers* established by its national supervisor as implemented in the jurisdiction where it is incorporated." Basel Framework CRE20.23 (emphasis added). Short-term bank exposures classified as Grade A are assigned a 20% risk weight. For a bank exposure that is ineligible for Grade A to be classified as Grade B and assigned a 75% risk weight, the bank "must meet or exceed the published minimum regulatory requirements *(excluding buffers)* established by its

2. RAA's proposed treatment of exposures to QICs under the ERBA

The RAA's risk-weighting proposal is based on the treatment of exposures to banks under the Endgame Proposal's ERBA. The RAA proposes to modify the ERBA to provide that the portion of any exposure that is covered by an eligible guarantee provided by a QIC, to the extent that the eligible guarantee meets the requirements of § __.120 of the ERBA,[34] must be assigned a 40%, a 75% or a 150% risk weight. These risk weights would *not* apply to direct exposures to QICs—only exposures arising under eligible guarantees, and only eligible guarantees meeting "substitution approach" requirements of § __.120 of the ERBA.

Under the RAA's proposal, a "Grade A" QIC eligible guarantee exposure, which would be assigned a 40% risk weight (subject to a floor, in the case of a foreign insurance company, equal to the risk weight assigned to sovereign exposures of the foreign insurance company's home country),[35] would be defined as follows:

> *Grade A qualifying insurance company exposure* means:
>
> (1) The portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company (to the extent that the eligible guarantee meets the requirements of § __.120) for which the qualifying insurance company is investment grade and exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator or foreign insurance regulator by an amount at least equal to the additional buffer percentage of the applicable minimum.
>
> (2) For purposes of paragraph (1) of this definition, *additional buffer percentage* means an amount, expressed as a percentage, equal to:
>
> (A) the minimum capital conservation buffer at or below which a [BANKING ORGANIZATION] is subject to limits on distributions and discretionary bonus payments under § __.11(a)(4); divided by
>
> (B) the minimum common equity tier 1 capital ratio under § __.10.
>
> (3) Notwithstanding paragraph (1) of this definition, an exposure is not a Grade A qualifying insurance company exposure if:
>
> (A) Data concerning the qualifying insurance company's compliance with the minimum risk-based capital, solvency capital, or similar requirements

national supervisor as implemented in the jurisdiction where it is incorporated." Basel Framework CRE20.26 (emphasis added). Short-term bank exposures classified as Grade B are assigned a 50% risk weight. A bank exposure that is ineligible for either Grade A or Grade B under the SCRA is classified as Grade C and assigned a 150% risk weight. *See* Basel Framework CRE20.29. Short-term bank exposures classified as Grade C are also assigned a 150% risk weight.

[34] *See* Endgame Proposal, 88 Fed. Reg. at 64203-64204 (§ __.120 of the proposed common rule) (setting forth rules of recognition for use of the "substitution approach" in the case of eligible guarantees and eligible credit derivatives, as well as required adjustments).

[35] Grade A QIC exposures that are self-liquidating, trade-related contingent items that arise from the movement of goods and that have a maturity of three months or less would be assigned a 20% risk weight.

established by its State insurance regulator or foreign insurance regulator have not been publicly disclosed within the previous 12 months;

(B) The qualifying insurance company's external auditor has issued an adverse audit opinion or has expressed substantial doubt about the ability of the qualifying insurance company to continue as a going concern within the previous 12 months; or

(C) For a foreign insurance company, the foreign insurance company is not domiciled and licensed in a foreign country that:

(i) is (or is a member state of) a jurisdiction subject to a covered agreement, or

(ii) is a reciprocal jurisdiction.

The definition of "Grade A qualifying insurance company exposure" generally corresponds with the definition of "Grade A bank exposure" in the Endgame Proposal's ERBA.[36] The "additional buffer percentage" concept is intended to treat QICs on a par with banking organizations and would be equal to (A) the minimum capital conservation buffer at or below which a banking organization is subject to limits on distributions and discretionary bonus payments under § __.11(a)(4) of the U.S. Basel III Regulations, divided by (B) the minimum common equity tier 1 capital ratio under § __.10 of the U.S. Basel III Regulations.[37]

The RAA's proposal would define a "Grade B" QIC eligible guarantee exposure, which would be assigned a 75% risk weight (subject to a floor, in the case of a foreign insurance company, equal to the risk weight assigned to sovereign exposures of the foreign insurance company's home country),[38] in terms similar to a Grade A qualifying insurance company exposure, except for the deletion of the "additional buffer percentage" definition and the modification of clause (1) of the definition to read as follows:

Grade B qualifying insurance company exposure means:

(1) The portion of any exposure that is covered by an eligible guarantee provided by a qualifying insurance company (to the extent that the eligible guarantee meets the requirements of § __.120) that is not a Grade A qualifying insurance company exposure and for which the qualifying insurance company is speculative grade or investment grade and meets or exceeds the minimum risk-based capital, solvency capital, or similar requirements established by its State insurance regulator or foreign insurance regulator.

[36] *See* Endgame Proposal, 88 Fed. Reg. at 64184-64185 (§ __.101(b) of the proposed common rule).

[37] Under the minimum capital conservation buffer and minimum common equity tier 1 capital ratio currently in effect, the additional buffer percentage would be $\frac{2.5\%}{4.5\%} \approx 55.56\%$.

[38] Grade B QIC exposures that are self-liquidating, trade-related contingent items that arise from the movement of goods and that have a maturity of three months or less would be assigned a 50% risk weight.

Under the RAA's proposal, a "Grade C" QIC eligible guarantee exposure, which would be assigned a 150% risk weight (subject to a floor, in the case of a foreign insurance company, equal to the risk weight assigned to sovereign exposures of the foreign insurance company's home country),[39] would be defined as a QIC eligible guarantee exposure that does not qualify as either a Grade A qualifying insurance company exposure or a Grade B qualifying insurance company exposure.

[39] Grade C QIC exposures that are self-liquidating, trade-related contingent items that arise from the movement of goods and that have a maturity of three months or less would be assigned the same 150% risk weight.