ACLI
Financial Security...for Life.

David Leifer
Vice President & Associate General Counsel

Jigar Gandhi
Counsel

Via E-Mail to regs.comments@federalreserve.gov

March 13, 2018

The Honorable Jerome Powell
Chair
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551

Re: Large Financial Institution Proposed Supervisory Guidance (Docket No. OP-1594)

Dear Chair Powell,

On behalf of the American Council of Life Insurers (the "ACLI"),[1] and its 290-member life insurance companies, we are writing in response to the request of the Board of Governors of the Federal Reserve System (the "Board") regarding the proposed guidance ("Proposed Guidance" or the "Proposal") to apply core principles of effective senior management, the management of business, lines, and controls for large financial institutions ("LFI"). We are pleased to engage in dialogue with the Board and other stakeholders on the development of appropriate ratings standards for LFIs.

The Board's proposed guidance is applicable to savings and loan holding companies (SLHCs) with total consolidated assets of $50 billion or more and systemically important nonbank financial companies ("SIFI") designated by FSOC for supervision. A component of ACLI's membership is subject to these parameters and therefore have a strong interest in the Board's proposed guidance.

Although the Board's recent proposed guidance is not the promulgation of new rules, we believe in line with previous ACLI comments, the Board's interpretative guidance is troublesome. ACLI believes that the specificity the Board proposes around specific functions and activities within LFIs does not allow for differing organizational constructs or account for the unique features of the various types of LFIs under the Board's jurisdiction. Further, the varying guidance from the Board, including elements of the LFI guidance, this proposed guidance, and guidance on Board of Directors' effectiveness, may create overlap. We request that the Board work to ensure that each of these proposals are harmonized to the greatest extent possible.

We further believe that any revised version of the Board's guidance should incorporate and leverage existing examinations from federal and state regulators. We appreciate the opportunity to provide comments and elaborate on our positions below.

[1] American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association with 290-member companies operating in the United States and abroad. ACLI advocates in state, federal, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for the financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing more than 95 percent of industry assets, 92 percent of life insurance premiums, and 97 percent of annuity considerations in the United States. Learn more at www.acli.com.

The Board's Proposed Guidance is Inappropriately Tailored to Insurance Companies

ACLI believes the Board inappropriately applies rules intended for banks to insurers who may be SLHCs or SIFIs. The proposed guidance cites existing statutes and states that a Chief Risk Officer ("CRO") must report to a Chief Executive Officer and to the Risk Committee of the company's Board of Directors, and further the Board cites to the risk management and reporting requirements for bank holding companies.[2] The Board also stipulates that a CRO must provide input to a company's Board of Directors on incentive compensation plans design and effectiveness. In this instance the Board is prescriptively applying a bank holding company regulation to non-bank financial institutions or inappropriately choosing the best functions and use of a company's CRO.

We believe that the Board should not mandate the specific functions of a CRO. To that end, we would request the Board change the proposed guidance to allow for oral or written reports from a CRO to the Risk Committee and refocus a CRO's input on compensation plans to whether it incentivizes excessive risk-taking. Decisions surrounding compensation plan design and effectiveness, are best left to a company's human resources department.

The Board's Proposed Guidance is Too Prescriptive

The Board's proposed guidance does not provide the necessary flexibility to insurance companies. In its objectives section, the Board states that the proposed guidance is "designed to delineate the roles and responsibilities for individuals and functions related to risk management."[3] ACLI requests that the Board change its focus in the proposed guidance to provide direction on what companies should do as opposed to prescribing how risk management activities should be done or whom should do it.

ACLI recommends that the Board look to existing frameworks for assistance when reworking its proposed guidance. The proposed guidance should follow the key principles set out by the National Association of Insurance Commissioners ("NAIC") Own Risk and Solvency Assessment ("ORSA") Guidance Manual. The Manual sets out five principles an insurer should include in any effective enterprise risk management framework: 1) Risk Culture and Governance; 2) Risk Identification and Prioritization; 3) Risk Appetite, Tolerances and Limits; 4) Risk management and Controls; and 5) Risk Reporting and Communications.[4]

Most pertinent in the Guidance Manual is the flexibility it affords insurers in their adoption of the principles. The Manual states specifically, "[t]he manner and depth in which the insurer addresses these principles is dependent on its own risk-management processes."[5] We believe here the NAIC provides the needed flexibility for various companies to tailor the principles to their specific risk management profile. We again request that the Board heed the NAIC's approach and update its guidance to provide direction and flexibility to companies.

The Board's Proposal Inappropriately Focuses Only on the Business Line as opposed to a Centralized Perspective

We believe that the Board's proposed guidance also assumes that certain responsibilities are undertaken by business lines which is not be true in all instances. For example, in the guidance, the Board writes: "[t]he activities of a business line should remain within risk limits established by IRM."[6]

---

[2] 12 CFR 252.33.
[3] Proposed Supervisory Guidance, 80 Fed. Reg. 1351 (January 11, 2018).
[4] NAIC Own Risk and Solvency Assessment Manual, available at, http://www.naic.org/store/free/ORSA_manual.pdf
[5] Id.
[6] Proposed Supervisory Guidance, 80 Fed. Reg. at 1358.

This statement and its adjoining footnote 39 assume that risk limits are established by individual business lines. This is not always the case, and the Board's proposed guidance should reflect that. In addition, the Board's proposed guidance inappropriately assumes that companies make determinations on training and development of staff by individual business lines. Many companies perform such functions centrally.

Further, the Board's proposed guidance stipulates that senior management govern a company's risk objectives and strategy across the enterprise level to ensure a company's soundness. However, in its referenced footnote 30, the Board infers that a company determines risk on a business line level rather than at the enterprise level.[7] We believe that in several instances of the Board's proposed guidance, it assumes that companies cannot undertake a new business or new initiative risk review at the enterprise level but must do so on the business line level. We again request that the Board's proposed guidance clarity that senior management may also determine risk on an enterprise level and not simply on a business line level.

In line with our comments above, under its Section titled "Core Principles of the Management of business lines" we request the following insertion (new language underlined): "For a LISCC firm, due to its size, risk profile, and systemic importance, these principles apply to all of the firm's business lines <u>as well as the overall enterprise</u>."

<u>Feedback to the Board's Specific Request for Comment</u>

Under the Board's specific requests for guidance, the Board states: "[o]ther supervisory communications have used the term ''risk appetite'' instead of risk tolerance. Are the terms ''risk appetite'' and ''risk tolerance'' used interchangeably within the industry, and what confusion, if any, is created by the terminology used in this guidance?" We believe here the Board assumes that the terms are interchangeable, which they are not. Risk Appetite is deemed to be the amount of specific risk(s), among many, the company chooses to accept and is comfortable with generally. Conversely, Risk Tolerance is the maximum amount of risk that a company can sustain.

In this vein, the Board in their proposed guidance states that "IRM should create lower-level risk limits, such as for an individual business line, based on the enterprise-wide risk limits." ACLI is unclear as to what the Board interprets as "lower-level risk limits" in its characterization. We request clarification or further definition.

<u>Specific Changes to the Language of the Proposed Guidance</u>

In accordance with the current U.S. insurance regulatory regime, we request the insertion of the term "lead" or "primary financial regulatory agency" in reference to the lead regulatory body for each company.

Under footnote 41, we request the insertion of the following language (underlined); "'Financial strength and resilience' is defined as maintaining effective capital <u>and loss absorption resources</u> and liquidity governance and planning process…"[8] We believe the added language provides a more comprehensive view of the critical components of financial strength and resilience. Insurer "loss absorption resources" go beyond just capital and provide a more accurate measure of a company's financial strength and resilience. We would also request the insertion of "loss absorption resources" in instances alluding to a company's financial strength throughout the proposed guidance.

[7] Proposed Supervisory Guidance, 80 Fed. Reg. at 1357.
[8] Proposed Supervisory Guidance, 80 Fed. Reg. at 1358.

In its discussion of internal controls, the Board refers to "[a]pprovals and appropriate dual authorizations for key decisions, transactions, and execution of processes." ACLI requests the deletion of the term "dual," since the number of authorizing bodies may vary per company. Simply changing the term to "appropriate" would suffice.[9]

Thank you for your consideration of these comments, and please contact should you have any questions.

Sincerely,

David M. Leifer

Jigar Gandhi

[9] Proposed Supervisory Guidance, 80 Fed. Reg. at 1362.