August 11, 2014

Robert deV. Frierson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Re: Amendments to the Capital Plan and Stress Test Rules (Docket No. R-1492 & RIN 7100 AE 20)

Dear Mr. Frierson:

I am submitting comments on behalf of a coalition of US insurance companies that are either supervised by the Federal Reserve or take a strong policy interest in rule makings affecting federally supervised insurers. We share certain perspectives with respect to the Federal Reserve Board's (the Board) implementation of Dodd-Frank stress tests for nonbank financial companies overseen by the Board (SIFIs) and savings and loan holding companies (SLHCs) substantially involved in the business of insurance. We appreciate the opportunity to submit comments on the Board's notice of proposed rulemaking (the Proposed Rule) amending the capital plan rule (the Capital Plan Rule) and stress testing rules (Stress Testing Rules) under the Board's Regulation YY, which implements Section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act).

I. Introductory Comments

The Board recently issued a final rule implementing certain enhanced prudential standards for bank holding companies and foreign banking organizations required by Section 165 of the Dodd-Frank Act (the Final Enhanced Prudential Standards Rule).[1] In the Final Enhanced Prudential Standards Rule, the Board refrained from implementing enhanced prudential standards for nonbank financial companies overseen by the Board in accordance with Title I of the Dodd-Frank Act (SIFIs) and, instead, stated that it would apply Section 165 enhanced prudential standards to designated SIFIs following an assessment of their business model, capital structure and risk profile.

We continue to urge the Board to pursue tailoring of any application of enhanced prudential standards to insurance companies, especially in stress testing rules that should reflect the differences between bank and insurance company business models. As the Board is aware, Section 165 of the Dodd-Frank Act specifically directs the Board to differentiate among companies on an individual basis or by category in prescribing more stringent prudential standards. The Board must take into account capital structure, riskiness, complexity, financial activities, size, and other risk-related factors the Board deems appropriate. On all these measures, insurance companies' business models, capital structures and risk profiles pose measurably different risks and require different treatment from bank holding companies, including in the formulation of capital stress testing models.

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1 Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 79 Fed. Reg. 17240 (Mar. 27, 2014).

The business models, capital structures and risk profiles of insurance companies differ significantly from the traditional bank holding company model, and supervisory stress tests should take these differences into account. For insurance organizations, a key concern is solvency and the ability to pay policyholders over long periods of time, in contrast to the short-term liabilities of banks. Premiums are collected in advance and invested ahead of anticipated claims, insurers have relative predictability of those claims, and insurance products have safety mechanisms, such as surrender charges, to protect against early liquidity demands. Unlike banks, which largely are funded by immediately payable deposits, insurers have longer-term liabilities and, therefore, find that longer-term assets, even those with higher short-term volatility, can often pose less risk and be a key component to long-term viability and financial strength of an insurer. For example, corporate debt securities represent the largest component of life insurer assets. In light of the insurance company liability structure, these substantial holdings of fixed income securities are risk-mitigating, rather than risk- enhancing.

In developing any capital planning or stress testing regime for insurers, we strongly encourage the Board to give careful consideration to the significant differences in capital structure and risk profile between banking organizations and insurance enterprises, particularly with respect to the key risks that are most likely to impact the capital position of the company. Insurance companies, for example, are exposed to mortality and casualty risk but pose less risk to counterparties and are generally less active in capital markets.

The business of insurance differs fundamentally from other areas of the financial services sector. The Coalition believes that the Board must account for the fundamental differences between insurance and banking to avoid damaging, unintended consequences for the insurance industry and the broader economy. We ask that the Board carefully consider the intent of Section 165 and written requests from Congress to accommodate the business of insurance in order to avoid any unnecessary negative impact resulting from its actions. Further, we encourage the Board to directly engage with the insurance industry to gather input and exchange ideas as final rules are developed.

II. Comments on the Proposed Rule

- **Timing of Actions in the Capital Plan and Stress Test Rules**

The Proposed Rule would shift the timing of the capital plan and stress cycles by one calendar quarter, subject to a transition period, in order to ease end-of-year resource constraints at covered companies. The Board correctly recognizes that the current timing obligates covered companies to conduct company-run stress tests and complete annual capital plans simultaneously with other financial reporting requirements, and notes that the process could be less onerous and costly if shifted away from other end-of-year filing requirements. We support this proposed change, especially with respect to covered companies that are substantially engaged in the business of insurance. Our companies may face resource constraints at the end of the calendar year, and would also benefit from a change in timing of capital planning and stress testing cycles.

- **Definition of Stress Scenarios**

The Proposed Rule would codify Board expectations regarding stress test scenario design by adding to the Capital Plan Rule the defined term "BHC Stress Scenario", i.e., a "scenario designed by a covered company that stresses the specific vulnerabilities of the company's risk profile and operations, including those related to the company's capital adequacy and financial condition."

We agree with the Board's assessment that previous supervisory scenarios were, "created with the overall banking industry in mind, rather than a focus on an individual company's risk profile," and we assume that any requirement for an insurance SIFI to design a stress testing scenario for purposes of the Capital Plan Rule will permit the development of scenarios that stress the "specific vulnerabilities" the insurer faces, e.g., mortality or catastrophe risk.[2] It would be inappropriate to apply stress scenarios designed for banking organizations to insurance companies.

- **Modifications to Capital Plan Resubmission Requirements under the Capital Plan Rule**

The Proposed Rule would remove the automatic requirement that a covered company resubmit its capital plan if objected to by the Board, and instead, would permit, rather than require, the company to resubmit its plan if it wishes to seek the Board's non-objection to its capital plan prior to the next capital plan cycle.

We support this proposed change, and believe it will provide needed flexibility for our companies to decide whether to resubmit plans.

- **Consequences for Failure to Execute Planned Actions under the Capital Plan Rule**

The Proposed Rule would amend the Capital Plan Rule to memorialize the Board's existing practices of approving repurchases of common stock on a net and gross basis and address other cases where a company fails to execute planned capital issuances in its capital plan. Specifically, the Proposed Rule would require that the net amount of a covered company's actual capital issuances and distributions be at least as great as net amounts projected in the company's capital plan, in each case for a given calendar quarter.

We respectfully suggest that the Board refrain from including this proposal in the final rule, and consider the merits of its current approach. A calendar quarter may be too short a period of time to impose such a constraint on capital actions in all instances. The Board should retain its authority to object to a capital plan on the basis of a failure to execute a previously planned capital issuance. The current approach provides the Board with greater flexibility while maintaining an incentive for companies to move forward with planned capital issuances as appropriate.

- **Clarification under the Capital Plan Rule of Capital Actions Not Requiring Approval**

The Proposed Rule would remove prior notice and approval requirements for distributions involving incremental issuances of instruments that qualify for inclusion in the numerator of a covered company's regulatory capital ratios. The Board states in the preamble to the Proposed Rule that removing this requirement will reduce unnecessary and burdensome efforts to submit requests for distributions outside of the capital plan process associated with issuances of regulatory capital.

We support this proposed change, and agree that subjecting incremental issuances to prior approval requirements is unnecessary and overly burdensome. In particular, mutual

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[2] 79 Fed. Reg. 37424.

insurance companies have limited options to raise equity in capital markets and sometimes rely on surplus notes for stable funding.

- **Provision of Supporting Models and Documentation**

The Proposed Rule would require a covered company to be capable of providing to the Board its loss, revenue and expense estimation models for stress scenario analysis, including supporting documentation regarding each model's development and validation status.

In addition, and consistent with the Board's approach in other contexts, we believe that SIFIs and SLHCs that are insurance enterprises should be provided with an adequate transition period to acclimate themselves to any Board requests for information in connection with the Capital Plan and Stress Testing Rules. We support the Board's decision to apply stress testing requirements to SIFIs only after specific notice[3] and to SLHC insurers, "in the year after the year in which the company becomes subject to the Board's minimum capital requirements."[4] Moreover, we encourage the Board to carefully consider the stress testing requirement as part of a larger regulatory burden our companies will become subject to simultaneously once subject to the Board's minimum regulatory capital requirements.

It is also our presumption that capital rules for nonbank SIFIs that are insurance companies and insurance-centric SLHCs would be finalized simultaneously in order to allow a uniform transition period for covered companies to Board oversight.

III. Final Remarks

We thank the Board for its consideration of our views and are available for further discussion of these matters as the Board works to finalize stress testing for insurance enterprises.

Sincerely,

Bridget Hagan

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[3] 79 Fed. Reg. 37423

[4] 79 Fed. Reg. 37422.