October 22, 2012

Via Federal eRulemaking Portal and U.S. Mail

The Honorable Thomas J. Curry
Comptroller
Department of the Treasury
Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219

The Honorable Martin J. Gruenberg
Acting Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20551

The Honorable Ben S. Bernanke
Chairman
Board of Governors of the Federal Reserve System
20th Street & Constitution Ave., NW
Washington, DC 20551

Re: Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action (FRS Docket No. R-1438 & RIN 3064-AD95); Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements (FRS Docket No. R-1442 & RIN 3064-AD96); Advanced Approaches Risk-Based Capital Rule; Market Risk Capital Rule (FRS Docket No. R-1442 & RIN 3064-AD97)

Dear Sirs:

We appreciate the opportunity to offer our comments in response to the Federal Reserve Board's (the "Board") notice of proposed rulemaking on Basel III (Basel III NPR or NPR 1) and the Standardized Approach for Risk-weighted Assets ("RWA") (Standardized NPR or NPR 2), collectively the "NPRs."

MetLife has been in the business of providing insurance for over 140 years and is a leading global provider of insurance, annuities and employee benefit programs serving 90 million customers. MetLife is the largest life insurer in North America (based on life insurance in-force). Through its subsidiaries and affiliates, MetLife holds leading market positions in the United States, Japan, Latin America, Asia Pacific, Europe and the Middle East. MetLife's clients include over 90 of the top 100 FORTUNE 500® companies. The MetLife companies offer life insurance, annuities, auto and home insurance, as well as group insurance and retirement and savings products and services to corporations and other institutions. MetLife's products and services are offered globally, through agents, third party distributors such as banks and brokers and direct marketing channels.

We are providing comments to the NPRs from the perspective of a holding company that is primarily engaged in insurance activities and with experience as a Bank Holding Company ("BHC"). Our position therefore provides a unique perspective on the application of banking standards to insurance companies, their relevance in managing safety and soundness of an insurance company, and the resulting business and competitive consequences. In addition, given that this framework has been developed for banking organizations, we have focused some of our more detailed comments on specific areas of concern that are most important and highlight where the framework is not appropriate for insurance companies.

- **We are primarily concerned that the Board may apply the risk-based capital standards proposed in these NPRs as part of the final Enhanced Prudential Standards for Systemically Important Financial Institutions ("SIFIs").** We reiterate the position made in our December 19, 2011 comment letter to the Financial Stability Oversight Council ("FSOC") and our April 30, 2012 response to the NPR on Enhanced Prudential Standards and Early Remediation Requirements for Covered Companies that MetLife and other insurance companies that substantially engage in regulated insurance activities should not be considered systemically important. We have taken an identical position in response to consultations by regulators who are evaluating global systemic risk assessment. However, if insurance companies are determined to be systemically important, we have significant concerns about the potential application of these risk-based capital standards to insurance companies. Further, current proposals for policy measures applicable to globally systemically important insurers ("G-SIIs") cause us concern that these risk-based capital standards could extend to US-based insurance groups designated as G-SIIs and further aggravate the competitive concerns raised below.

  The banking capital framework proposed in NPR 1 and NPR 2 fundamentally does not address the unique risk profile and business model of insurance companies. An insurance company's liabilities are the primary determinant of its overall risk profile and drive its investment decisions, assumption of credit risk and its liquidity risk exposure. As a liability driven business, insurance often has long term cash flow patterns, and an insurance company's investment portfolio composition and credit quality distribution is highly linked to and driven by the liability profile of its insurance products. By mostly ignoring the linkage between assets and liabilities and focusing on assets as the primary basis for determining capital requirements, the proposed capital framework fails to reflect the business model and risk profile of insurance companies. While NPR 2 notes specific adjustments to the banking capital framework for insurance-related activities, these adjustments are either inappropriate for insurance companies or only address distinct asset areas and do not holistically capture the direct linkage between asset and liability management and therefore the overall management of capital at insurance companies.

We reiterate that U.S. insurance companies are heavily regulated and have long-standing capital and liquidity frameworks that generally have been effective and have evolved in light of past crises through regulatory responses. These insurance-specific frameworks have contributed to mitigating the impact of insurance company failures in the past. The failure of a large insurance enterprise during the most recent financial crisis did not involved regulated, traditional insurance activities, but instead non-traditional banking activities involving complex financial products conducted outside of the firm's regulated insurance entities.

- **We have significant concerns that the application of the proposed rules in NPR 1 and NPR 2 to insurance companies would penalize the insurance business model in a manner that is disproportionate to the actual risk.** For example, the application could lead some insurance companies to revise their portfolio structure to focus on assets that minimize capital requirements under the proposed rules, but such revisions may not be appropriate for the associated liabilities. The application could also lead to other unintended consequences including increased product costs to insurance customers and even possibly curtailment of the availability of certain insurance products. Such decisions would adversely impact the public interest, most notably the interests of insurance customers, be inconsistent with prudent capital management and not serve to enhance the safety and soundness of the US financial system, outcomes most certainly counter to the intent of the proposed regulations and the enabling law.

- **The selective application of the proposed rules to only those insurance organizations subject to Federal Reserve supervision, either currently as Savings and Loan Holding Companies ("SLHC"), BHC, or potentially as non-bank SIFIs, could create a competitive disadvantage for these insurance companies relative to the significant portion of the insurance market that would remain under existing insurance capital standards, including U.S peers and foreign insurance companies.**

- **We recommend that the Board undertake a comprehensive quantitative review of the proposed capital framework.** This comprehensive review could be structured similar to the Quantitative Impact Studies undertaken for banks, but would utilize insurance-specific data and experience. Its primary objective should not only be to measure the impact of specific components of the proposed capital rules but also to lay the groundwork for an assessment and development of a more appropriate capital framework for insurance companies.

Our review of the proposed rules highlights specific areas of concern in the NPRs that are described at a high level below and in Appendix A. While our comments focus on specific components, we reiterate that the proposed capital framework needs to be revisited holistically in order to more fully address the risk profile of insurance companies.

Insurance Related Activities in Standardized NPR:

- **Recommend removal of the insurance subsidiary capital deduction:** The disallowance of minimum capital levels at insurance underwriting subsidiaries is not appropriate for companies where insurance underwriting accounts for a majority of revenue and balance sheet items. The deduction causes double counting of capital requirements as related assets in these subsidiaries would also be included in the RWA calculation. While we recognize that the proposed rules were designed with banking organizations in mind and may be appropriate for banks with small insurance companies, we recommend that this deduction be removed where insurance is the predominant activity of a banking holding company group. Requiring a deduction of the insurance capital under these circumstances eliminates a large proportion of the group capital in a manner that is inconsistent with the actual risk profile.

- **Recommend change to the definition and RWA approach for Separate Account Assets:** While we generally agree with the proposed definition of a Separate Account, we recommend that the proposed wording to qualify a non-guaranteed separate account[1] be removed from the proposed rules as it does not align with the definition of non-guaranteed separate accounts from state insurance regulators and US generally accepted accounting principles (US GAAP). If the definition remains the same as in NPR 2, we recommend a risk weight of 0% for the related assets, as described in Appendix A. Similarly, we recommend a risk weight of 0% for accounts that do not qualify for separate account treatment as long as all credit risk is borne by the policyholder.

- **Recommend 0% risk weight for Policy Loans:** The Standardized NPR does specifically address policy loans, which were not addressed in the General Risk-based Capital Rules. However, a risk weight of 20% does not reflect the true risk of this asset type. We reiterate our recommendation from our April 30, 2012 response to the Enhanced Prudential Standards NPR that a 0% risk weight be applied to policy loans since there is no credit risk related to these assets as they are fully collateralized. Policy Loans represent loans made to policyholders and are less than or equal to the existing cash surrender value of their respective policies. The policy loan asset is backed by the policyholder's cash surrender value which is a liability to the company. If the policyholder defaults on the loan, the company can write down the liability (i.e. pay less benefits). This would happen in a normal or distress situation. A collateralized debt, on the other hand, is backed by some other assets for which the company is still exposed to credit risk, which is not the case for policy loans, which are naturally offset by the company's liability.

Additional comments on Standardized NPR:

- **Recommend revisiting the RWA approach for Securitization Exposures:** We have a number of concerns about the proposed Simplified Supervisory Formula Approach ("SSFA") for calculation of capital requirements for securitization products as discussed in Appendix A.

[1] From NPR 1 page 86 – "To qualify as a non-guaranteed separate account, the insurance company could not contractually guarantee a minimum return or account value to the contract holder, and the insurance company would not be required to hold reserves for these separate account assets pursuant to its contractual obligations on an associated policy."

For example, the calculation of K_G[2] for Residential Mortgage Backed Securities ("RMBS") products is very cumbersome as the information needed to classify the underlying exposures as either Category 1 or Category 2 residential mortgage exposures is not readily available for investors in RMBS products. In addition, the SSFA would be one of the largest impacts in terms of percentage increase to RWA relative to Basel I for insurance companies, which could impact the appetite that insurance companies have in continuing to invest in these products.

- **Recommend differentiating risk weights for Corporate Bonds:** The proposed 100% risk weight for corporate exposures does not distinguish between higher quality and lower quality corporate bonds. This lack of differentiation impacts insurance companies more than banks as they have a significantly higher share of corporate bonds in their investment portfolios. We recommend that the Board modify the proposed rule under NPR 2 and assign differentiated risk weights for Corporate Bonds by potentially leveraging the risk weights assigned for such exposures in the final Risk-Based Capital Guidelines for Market Risk (Market Risk Final Rule).

- **Recommend exclusion of Separate Account assets in the calculation of Tier 1 Leverage:** We reiterate our recommendation to exclude assets held in custodianship, such as Separate Account balances, for the calculation of the Tier 1 Leverage Ratio. These Separate Account asset balances are matched directly against Separate Account liabilities and do not have an impact on the financial leverage of the insurance company. Therefore, when assessing the leverage ratio, Separate Accounts should be excluded from the calculation and considered offset by the related liabilities.

Comments on Basel III NPR:

- **Recommend exclusion of unrealized gains/losses on Available for Sale ("AFS") securities in Tier 1 Capital:** We reiterate in this comment letter that the proposed capital treatment of unrealized gains/losses on AFS securities in the Basel III NPR introduces unnecessary volatility to the capital ratios especially for insurance companies and should remain an exclusion from Tier 1 Capital similar to Basel I regulatory capital calculations. Insurance companies are more likely to retain the assets in their investment portfolios for a long time since these assets back long-dated liabilities. Therefore, during times of crisis, insurance companies are not compelled to sell assets and realize losses due to temporary market movements. When credit events do occur, insurance companies follow the normal OTTI process to which banks are also subject. In addition, because liabilities are recorded at book value under current accounting rules, any decline in the value due to a rise in interest rates is not recorded on the financial statements. Hence, in a rising interest rate environment, insurance companies would experience an increase in unrealized losses on their investment portfolios without recognizing an accounting offset for the corresponding gain resulting from the decline in the value of policyholder liabilities. Proposed treatment in the APRs would inappropriately raise or lower regulatory capital with minimal, if any parallel change in risk.

[2] NOTE: K_G refers to the weighted average total capital requirement of underlying exposures calculated using the standardized approach risk-based capital rules.

- **Propose revisiting the application to insurance of the 2.5% capital conservation buffer as well as expanding measures of qualifying capital towards minimum capital requirements:** We propose that the Board revisit the use of 2.5% as the capital conservation buffer for insurance companies since the analysis and discussion to support this level focused on the banking industry's experience in past economic crises and it does not appear that a comparable analysis was performed to determine what would be an appropriate capital conservation buffer above the minimum for the insurance sector.

  Moreover, the Board should consider other buffers available to insurance companies that could provide significant loss absorption in times of stress. Examples include Provisions for Adverse Deviations ("PADs") and the dividend margin present in several of our products especially the Closed Block.

  PADs are provisions for the risk of adverse deviation from "best estimate" assumptions in the measurement of liabilities for future claims and policy benefits. They are always positive and have the ability to provide loss absorption similar to that for a bank's Allowance for Loans and Leases.

  A Closed Block is a specific set of invested assets allocated for the benefit of a set of policies, referred to as a "closed block". At the time of set-up, insurance companies define a dividend scale based on operating experience at the point of demutualization. This dividend scale can be adjusted and even eliminated depending on actual experience relative to expected cash flow and operating earnings set out at demutualization for the closed block. This structural feature (i.e., ability and expectation to adjust dividend) provides significant loss absorption since it reduces liabilities if asset performance, including credit losses, is worse than expected.

Appendix A expands on our specific comments in greater detail and Appendix B provides more background on the risk profile of insurance companies.

Thank you for considering our comments. We hope that these comments prove helpful to the agencies with this rulemaking. If you have any questions concerning the views expressed in this letter, please feel free to contact me. Adapting regulations such as these to appropriately accommodate the business of insurance is a complicated and difficult task, but it is important that a good outcome be achieved. We would be pleased to discuss our comments with you, provide any additional information you might need and/or collaborate with you to assist in the further development of the regulations.

Respectfully submitted,

Nicholas D. Latrenta

Executive Vice President & General Counsel

APPENDIX A

Considerations for changes to the proposed capital requirements in the Basel III and Standardized NPRs if applied to insurance companies due to the unique business model and risk profile of insurance companies

We believe that the proposed capital framework should be revisited holistically to consider the impact on insurance companies. This can be achieved by conducting a comprehensive Quantitative Impact Study ("QIS") of the Integrated Capital Framework on insurers.

In advance of a more comprehensive QIS, several elements of the Basel III framework and the Standardized Approach to RWA are not appropriate to the business model and risk profile of insurance companies and should be modified if the banking capital framework were to be applied to insurance companies. Described in more depth below are the proposed modifications for both the Standardized NPR and Basel III NPR.

1) Standardized Approach – Insurance Related Activities

The Standardized NPR contains proposals to adapt the banking capital framework for insurance related activities. However, the proposed changes do not holistically address differences between the risks of insurance companies and banking organizations and would have unintended consequences if applied to insurance companies. Three areas that we have specific comments on include:

a) Recommend removal of the insurance subsidiary capital deduction rule

The Standardized NPR proposes an additional deduction of the minimum regulatory capital requirement of insurance underwriting subsidiaries [generally 200 percent of the subsidiary's authorized control level as established by the appropriate state insurance regulator] from total capital to reflect the capital needed to cover insurance risks. We strongly recommend that this deduction be removed from the final rule.

As noted in our April 30, 2012 response to the Enhanced Prudential Standards NPR, during the proposal stages of Basel II, several commenters objected to the proposed deduction from Tier 1 capital by noting that it was overly conservative and resulted in a double-count of capital requirements for insurance regulation and banking regulation. Local insurance regulatory capital minimums already have a required capital component for credit risk (e.g., C1 is the statutory RBC version of credit risk in the U.S.). By deducting this amount (plus balances for market, insurance and operational risk) out of Tier 1 capital for Basel III purposes, the commentators argued correctly that the consolidated BHC may have to reserve additional capital to cover these assets, despite the fact that they are already provided for in the statutory RBC calculation.

In response, the Board noted that the capital requirements imposed by a functional regulator reflect capital needs at the particular subsidiary, while the consolidated measure of minimum capital requirements reflect the consolidated enterprise. Recognizing that this deduction was included in the rules to minimize any potential regulatory capital arbitrage and ensure there is adequate capital at the consolidated level, such treatment is more suitable to traditional banking institutions with smaller insurance underwriting activities.

For companies where insurance underwriting accounts for a majority of revenue and balance sheet items, the combined impact of a deduction of insurance subsidiary capital and the inclusion of insurance subsidiary assets in the overall RWA calculation would significantly impact the calculation of risk-based capital ratios. This deduction would severely deplete the amount of available capital for regulatory capital ratios of insurance companies and does not appropriately measure the risk of those companies. We recommend that the deduction be removed.

b) Recommend changes to RWA approach for insurance-related activities

The Standardized Approach addresses certain nonbanking exposures that were not explicitly identified or assigned specific risk weight categories under the general risk-based capital rules (Basel I). However, some of the proposed risk weight treatments in NPR 2 do not appropriately align with the risk of the assets within the insurance-related activities, because unlike a bank, certain components of asset returns and losses are passed through to the policyholders. Therefore, we recommend changes to the proposed Standardized Approach for risk weighting the following insurance-related activities in order to appropriately reflect their risk profile[3].

i) Separate Account Assets[4]

> *Question 20: The agencies request comment on how the proposed definition of a separate account interacts with state law. What are the significant differences and what is the nature of the implications of these differences?*

We generally agree with the proposed definition of a Separate Account in the Standardized NPR, including the four conditions that must be met to be considered a Separate Account. In addition, we agree with the proposed zero risk weight for assets held in non-guaranteed separate accounts.

However, the NPR includes criteria for non-guaranteed Separate Accounts that do not align with US GAAP related to Separate Accounts, as defined by the AICPA in ASC 944-80, or with guidance issued by the National Association of Insurance Commissioners (NAIC). Specifically, the following statement within the definition of a non-guaranteed separate

3 Ibid, Comments Section D, Proposed capital requirements for certain nonbanking exposures, page 14.
4 Separate accounts represent assets that are typically maintained by a life insurance entity for purposes of funding obligations to individual contract holders under fixed-benefit or variable annuity contracts, pension plans, and similar contracts. The contract holder generally assumes the investment risk, and the insurance entity receives a fee for investment management, certain administrative expenses, and mortality and expense risks assumed. A separate account is not a distinct legal entity, but rather an accounting entity created by and under the control of an insurance entity that owns 100 percent of the assets held in the separate account. The separate account arrangement legally isolates certain assets backing variable contracts from the other assets of the insurance entity (the other assets of the insurance entity are held in the general account of the insurer). The main reason for this structure is to protect assets backing the separate account component of variable contracts from the general creditors of the insurance entity if the insurance entity becomes insolvent, FASB, Acct. Standards Update (No.2010-15), April 2010, pp.1-2.

account on Page 86 of the Standardized NPR does not align with US GAAP or NAIC guidance:

> *"To qualify as a non-guaranteed separate account, the insurance company could not contractually guarantee a minimum return or account value to the contract holder, and the insurance company would not be required to hold reserves for these separate account assets pursuant to its contractual obligations on an associated policy."*

Insurance companies that offer variable annuity products with investments in Separate Accounts often include a guarantee of minimum benefits related to the annuity products. Volatility in the value of the Separate Accounts assets vs. the guarantee amount is captured through the valuation and posting of related liabilities, which are regularly revalued and may result in holding reserves. Thematic guidance recognizes this form of Separate Account as non-guaranteed for accounting purposes and for the determination of the asset charge in the risk-based capital (RBC) formula, but the wording in the Standardized NPR would suggest that these same products be considered guaranteed under the NPR. The NAIC issued Statement of Statutory Accounting Principles (STAT) No. 56 on Separate Accounts in 2000, which defines nonguaranteed separate accounts as:

> *"Variable separate accounts, where the benefit is determined by the performance and/or market value of the investments held in the separate account. Include variable accounts with incidental risks, nominal expense, and minimum death benefit guarantees."*

Therefore, the NAIC guidance includes separate accounts with minimum death benefit guarantees and other guarantees as non-guaranteed separate accounts. The NAIC recognizes risk inherent in the guaranteed benefit, but that risk is assessed through a reserve liability held in the general account. Statement No. 56 states:

> *"Where a variable annuity contract or variable life insurance contract contains a guaranteed minimum death benefit, any reserve liability for such death benefit provision shall be recorded and held in the general account based on the reserving guidance in paragraphs 25 and 26. Any differences between the benefit paid and the separate account asset value of the contract shall be charged against or credited to the general account in its net gain from operations."*

The difference in definition between the Standardized NPR and NAIC guidance has significant implications for the calculation of risk-based capital requirements for insurance companies. The definition in the Standardized NPR could force a large amount of assets to be considered guaranteed and risk weighted, even though the same assets would be considered non-guaranteed by US GAAP and NAIC guidance. Based on an assessment of MetLife's portfolio under the proposed definition, the wording in the NPR would result in extremely punitive RWA treatment for the underlying assets. We recommend that the additional criteria on non-guaranteed Separate Accounts referenced above be removed.

Approach to Assess Risk for Separate Accounts with Guaranteed Benefits

We recognize that the definition of non-guaranteed Separate Accounts in the NPR may remain as it is; in that case, we would recommend revisiting the approach to assess capital requirements for the related assets by consideration of the US GAAP liability recorded for these exposures. The section below discusses the products in more detail and the approaches used by insurers to assess the risk.

Unlike other financial institutions, the liabilities that insurers write would rarely cause a liquidity issue ("run on the bank scenario") due to the fact that the liabilities are almost never due on demand. The variable annuity products included in the Separate Accounts often offer minimum benefits, which could take the form of a life benefit which requires a long waiting period (on average, 10 years) before *any* benefit can be received. Once the payouts begin, they typically have a 20 year payout period. These benefits are initially funded by the policyholder's own assets. If the guarantee exceeds the assets available once the payouts begin, the insurer funds the shortfall. Therefore, there is a long time over which the insurer is able to recover the shortfall. In most cases, there is a 10 year certain period, and when the policyholder dies, the payments cease.

Many of the variable annuities also offer a death benefit, which would be paid out immediately at death but overall payouts for these products depend on several assumptions about the population that may be entitled to receive these benefits. Therefore, the valuation of liabilities for US GAAP considers many assumptions around the likelihood and potential timing of the minimum benefits in addition to any movement in the Separate Account balance relative to the guarantee. If the Separate Account balance is not sufficient at a point in time to cover the minimum guarantee, that shortfall is considered against assumptions as to when the shortfall could actually impact the insurance company given the long payout period for these guarantees.

US GAAP reporting relies on ASC 815 (formerly FASB Statement 133) and/or ASC 944-20 (formerly SOP 03-1) which defines the requirements for calculating the liability. ASC 944-20 states that any liabilities related to minimum guarantees and insurance benefit liabilities under the contracts in excess of the fair value of separate account assets representing contract holder funds should be recognized as general account liabilities. If the guarantees meet certain criteria, rather than being valued under ASC 944-20 guidance, they are bifurcated from the host contract as required by ASC 815 and valued under fair value reporting requirements per ASC 820 (formerly FASB Statement 157). These fair value calculations consider a number of different scenarios and apply assumptions with respect to expected equity market and interest rate volatility, mortality, morbidity, persistency, and expenses. Whichever accounting measurement and presentation method is used, it is our opinion that the US GAAP liability for these exposures is sufficient to provide for the associated risk so no additional capital should be required for the Separate Account assets related to these accounts even if they are considered guaranteed according to proposed criteria.

The punitive effect of this capital charge would directly impact the industry's ability to write this business. Additionally, this effect on the business could result in a reduction in the availability of a high demand product and/or significantly increase the price to support the additional cost of the required capital. These unintended impacts need to be carefully considered when finalizing any rule.

Finally, we also recommend a risk weight of 0% for accounts that do not qualify for separate account treatment as long as all credit risk is borne by the policyholder.

ii) <u>Policy Loans</u>

The Standardized NPR assigns a 20% risk weight to Policy Loans. We reiterate our recommendation from our April 30, 2012 response to the Enhanced Prudential Standards NPR that a 0% risk weight be applied to policy loans since there is no credit risk related to these assets as they are fully collateralized. Policy Loans represent loans made to policyholders and are less than or equal to the existing cash surrender value of their respective policies. The policy loan asset is backed by the policyholder's cash surrender value which is a liability to the company. If the policyholder defaults on the loan, the company can write down the liability (i.e. pay less benefits). This would happen in a normal or distress situation. A collateralized debt, on the other hand, is backed by some other assets for which the company is still exposed to credit risk, which is not the case for policy loans, which are naturally offset by the company's liability. Therefore there is no credit risk related to policy loans, and these should receive a risk weight of 0%.

2) Standardized Approach – Additional Comments

Proposed rules in the Standardized Approach for banking-related activities do not appropriately measure the risk of the asset types or significantly impact insurance companies and therefore would affect the competitiveness of insurers that apply the rules as discussed in the key examples below:

a) Recommend revisiting the Simplified Supervisory Formula Approach (SSFA) and due diligence requirements for Securitization Exposures

Overall, the SSFA causes much higher risk-weighting of securitization products in which MetLife and other insurers are large investors. In addition, the SSFA requires additional information that is not all readily available from public sources. We believe that these new rules could have substantial unintended impacts on the competitiveness of insurance companies that apply the rules as compared to insurance companies that are not subject to them. For MetLife and other insurance companies, this transition is one of the largest percent increases for risk-weighted assets relative to Basel I and could force many insurance companies to re-evaluate their investment participation in certain markets.

We have the following concerns and specific recommendations related to SSFA and the due diligence requirements:

i) Category 1 v. Category 2 for Residential Mortgage Backed Securities (RMBS) Securitization The calculation of K_G for RMBS products is very cumbersome as the information needed to classify the underlying exposures as either Category 1 or Category 2 residential mortgage exposures is not readily available for investors in RMBS products. In particular, the requirements related to verification of underwriting standards are usually only available to the originator of the mortgages and not the investor in related securitization products. Additionally, some mortgage originators are not currently in business so the underlying information may not be available at all. Therefore, the requirements around the verification of underwriting standards are unreasonable at this time, especially for securitizations based on residential mortgages originated in the past. We recommend that mortgages originated prior to 2015 be grandfathered for purposes of calculating K_G in the SSFA, where K_G for mortgages originated prior to 2015 is determined utilizing the general risk-based capital rules. This will allow adequate time for the industry to require securitization originators to make the information required to classify the underlying mortgages as Category 1 or Category 2 available in the prospectus, trustee, and servicer documentation.

ii) Overcollateralization – We recommend that the final rules clearly articulate that overcollateralization ("OC") is included in the attachment point for SSFA. Given the updated definition of attachment point in the Standardized NPR as compared to the previous Market Risk NPR, we assume that OC can be included as the wording changed from "the dollar amount of the [subordinated] securitization positions" to "the dollar amount of [subordinated] underlying exposures". Exclusion of OC would ignore the significant role this provision has in providing credit protection to all investors, including the most subordinated positions.

iii) Discount From Par – Reinforcing previous industry comments, we recommend that the attachment point parameter of a securitization position include any discount from par under the SSFA. The discount from par should be considered as additional credit enhancement as it more closely aligns the true credit risk of the position to the amount of risk-based capital to be held against the securitization exposure.

iv) Re-securitization – The calculation of RWA for re-securitizations is highly labor intensive given the lack of readily available information and the time required to perform the calculations. Given the difficulties in obtaining information noted above, this difficulty is compounded for re-securitizations. Additionally, the supervisory calibration parameter (p) is not risk-sensitive as it imposes an overly punitive capital charge regardless of the percent of the underlying collateral that are securitizations. We agree with other industry comments that suggest a de-minimis bucket where, if the underlying collateral of a securitization deal contain less than 5 percent securitizations, the deal is not considered a re-securitization for purposes of determining the supervisory calibration parameter in the SSFA. In addition, deals in which a single securitization position is securitized to create additional tranches should not be classified as a re-securitization and receive a p value of 1.5. These deals simply amend the existing capital structure in order to further customize the credit and/or interest rate risk of a single tranche based on the risk/return preferences of additional investors, as opposed to creating the cross deal complexity inherent in true re-securitizations.

v) Federal Family Education Loan Program ("FFELP") Student Loans– Reinforcing previous industry comments, we recommend that student loans in forbearance or deferment would not be included in parameter W in the SSFA calculation. We believe that these loans should not be considered as having "contractually deferred" interest payments if interest payments are deferred due to the borrower's student status (e.g., still in school, in grace period after graduation, or in deferment based on a student's return to school to complete a degree or conduct post-graduate study). The inclusion of these loans in parameter W would be inappropriate as student loans are structured to defer a borrower's payments during specified periods to accommodate situations unique to higher education.

vi) Due Diligence Requirements – We request clarification on the level of documentation required to demonstrate due diligence performed before investing in securitization products and related quarterly due diligence during the investment holding period. Similar to most institutions, we believe we perform due diligence that is commensurate with the complexity of the securitization exposure and the materiality of the position in relation to capital; however, we are unsure of the agencies' expectations regarding documentation for this standard.

b) Recommend to differentiate risk weights for corporate bonds

The Standardized Approach NPR does not distinguish between higher quality and lower quality corporate bonds as these assets receive standard 100% risk weights. Since insurance companies have a significantly higher share of corporate bonds in their investment portfolios compared to banks, insurance companies are more negatively affected by this lack of differentiation and insurance companies that are subject to the rules would be at a competitive disadvantage. We recommend that the Board modify the proposed rule under NPR 2 and assign differentiated risk weights for Corporate Bonds by potentially leveraging the risk weights assigned for such exposures in the final Risk-Based Capital Guidelines for Market Risk (Market Risk Final Rule). The Market Risk Final Rule provides an Alternative Measure for Corporate Debt Positions that addresses the following categories of corporate bonds, for example:

i) Corporate debt positions issued by depositary institutions, foreign banks and credit unions – specific risk weight factors range between 0.25% to 12% and are assigned based on the rating of country of incorporation as well as the position's remaining maturity;

ii) Corporate debt positions under the investment grade methodology – specific risk weight factors assigned based on investment grade category and remaining contractual maturity (range between 0.5% to 4% for investment grade and 12% for non-investment grade); and

iii) Corporate debt positions issued by private companies – specific risk weight factor of 8% used for all.

c) Recommend exclusion of Separate Account assassinate calculation of the Tier 1 Leverage Ratio

We reiterate our recommendation from our April 30, 2012 response to the Enhanced Prudential Standards NPR for the Board to consider the exclusion of assets held in custodianship, such as Separate Account balances, for the calculation of the Tier 1 Leverage Ratio.

The principal objective of the Tier 1 Leverage measurement is to place a constraint on the degree to which a banking organization can leverage its equity capital base. The metric is used as a supplement to the Basel RBC ratios. As stipulated in the FSOC's second NPR entitled "Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies," 12 CFR Part 1310, Separate Account assets are excluded from the leverage and short term debt ratios. These exclusions are due to the fact that such accounts are not available to satisfy claims of general creditors. A related exclusion for Separate Account asset balances should be extended to the 12 CFR part 225 calculation of Tier 1 Leverage. Such an exemption would be consistent with the intent of the leverage ratio as these Separate Account asset balances are matched directly against Separate Account liability accounts and do not have an impact on the financial leverage of the insurance company. Therefore, in assessing the leverage ratio, Separate Account should be excluded from the calculation and considered offset by the related liabilities.

3) Basel III NPR (Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action)

Certain requirements proposed in the Basel III NPR would likely have a larger impact on insurers than traditional banking organizations, as discussed in key examples below. The section below also includes other areas in the Basel III NPR that would likely concern both banking organizations and insurers.

a) Recommend exclusion of unrealized gains/losses on AFS securities in Tier 1 Capital:

We reiterate our recommendation from our April 30, 2012 response to the Enhanced Prudential Standards NPR to remove the effect of unrealized gain/loss on Available for Sale ("AFS") securities from the calculation of available regulatory capital due to the temporary nature of such gain or loss and the unnecessary volatility that this introduces to the capital ratios of an insurance company, which generally hold long-dated investment assets to back long-dated liabilities.

Unrealized gains/losses are included under Basel III for the purpose of calculating Tier 1 common, Tier 1 capital and Total risk-based capital. Per Page 49 of the Basel III NPR: "Under the agencies' general risk-based capital rules, unrealized gains and losses on AFS debt securities are not included in regulatory capital, unrealized losses on AFS equity securities are included in tier 1 capital, and unrealized gains on AFS equity securities are partially included in tier 2 capital. As proposed, unrealized gains and losses on all AFS securities would flow through to common equity tier 1 capital. This would include those unrealized gains and losses related to debt securities whose valuations primarily change as a result of fluctuations in a benchmark interest rate, as opposed to changes in credit risk (for example, U.S. Treasuries and U.S. government agency debt obligations).

The inclusion of unrealized gains and losses in the calculation of regulatory capital under Basel III poses unique challenges for an insurance company since, compared to a typical bank, a significantly larger percentage of its assets are investment securities classified as AFS and carried at fair value. As a result, under Basel III an insurance company's capital position will be particularly sensitive to changes in interest rates and credit spreads due to the long term nature of its liabilities and therefore its invested assets. In addition, liabilities are recorded at book value and, under current accounting standards any decline in the value due to a rise in interest rates is not recorded on the financial statements. Hence, in a rising interest rate environment, insurance companies would experience an increase in unrealized losses on its investment portfolio without recognizing an accounting offset for the corresponding gain resulting from the decline in the value of policyholder liabilities.

Our primary recommendation is to remove the effect of unrealized gain/loss on AFS securities from the calculation of available regulatory capital. The rationale is as follows:

- Insurance companies are more likely to retain the assets in their investment portfolios for a long time since these assets back long-dated liabilities. Therefore, during times of crisis, insurance companies are not compelled to sell assets and realize losses due to temporary market movements. When credit events do occur, insurance companies follow the normal OTTI process to which banks are also subject. Proposed treatment would inappropriately raise or lower regulatory capital with minimal, if any parallel change in risk.

- The inclusion of unrealized gain/loss introduces substantial volatility to regulatory capital ratios which may undermine market confidence. This volatility is estimated to be three to six times greater for insurance companies relative to banks due to the larger percentage of insurance assets in the AFS book.

It is also important to note that current expected changes to accounting rules governing insurance contracts[5] will largely offset the unrealized gain/loss starting 2016/2017 by carrying insurance liabilities at market consistent values. As an alternative to the primary recommendation above, if the Board decides to retain the current rule around unrealized gain/loss, we recommend that the economic movement in liability values associated with unrealized gain/loss, due to interest rate movements be reflected, until such time the accounting for insurance contracts reflects the offset.

b) ***Propose revisiting the application to insurance companies of the 2.5% capital conservation buffer:***

We request that the Board revisit the 2.5% level as the fully phased-in capital conservation buffer to assess whether this level is appropriate for insurance companies given that the determination of this level of buffer may have been based on history related to only the banking industry. It does not appear that a comparable analysis was performed to determine what would be an appropriate conservation buffer above the minimum for the insurance sector in relation to the losses experienced in the crisis.

4) Insurance-related Activities not Addressed in the NPRs

Finally, the Standardized NPR and Basel III NPR do not address important insurance-related activities that should be considered in a regulatory capital framework applied to insurance companies. Two examples are discussed below.

a) ***Propose inclusion of Provision for Adverse Deviations (PADs) as a buffer that can provide significant loss absorption in times of stress:***

As noted previously, the proposed rules do not holistically look at both the assets and liability side of the balance sheet for insurance companies. This requirement is essential for insurance companies when determining their capital ratios due to the nature of the insurance industry.

In considering both assets and liabilities, we recommend that the Board consider including Provisions for Adverse Deviation (PADs) as a buffer that can provide significant loss absorption in times of stress. PADs are provisions for the risk of adverse deviation from "best estimate" assumptions in the measurement of liabilities for future claims and policy benefits. According to FAS 60, the risk of adverse deviation is defined as:

"A concept used by life insurance enterprises in estimating the liability for future policy benefits relating to long-duration contracts. The risk of adverse deviation allows for possible unfavorable deviations from assumptions, such as estimates of expected investment yields,

[5] The Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) are developing a new accounting standard for insurance contracts. The proposed framework would introduce market consistent components for the valuation of insurance liabilities. The liability would be reported each period as the present value of the current estimate of future cash flows (premiums less claims and certain direct expenses). The discount rate will be re-measured each reporting period using current interest rates determined based on the characteristics of the liability. Within this framework, the impact of change in discount rates on the insurance liability would flow through Accumulated Other Comprehensive Income (AOCI) similar to unrealized gain/loss on AFS related to interest rate movements. The industry expects an exposure draft from the FASB and a re-exposure draft from the IASB in the 1st quarter of 2013 with implementation timing expected for 2016 or 2017.

mortality, morbidity, termination, and expenses. The concept is referred to as risk load when used by property and liability insurance enterprises."

As a result, this reserve assumption is more conservative relative to "best-estimate" assumptions. If actual experience unfolds in accordance with the "best-estimate" expectations, additional profit will emerge as the PAD is released. For example, if interest rates are higher than assumed in reserving, a spread is created because investment income on assets supporting the benefit is greater than the interest needed to fund the benefit reserves. US GAAP profits will materialize due to the gross premiums and to the release of the margin in the assumptions causing the profits as a percentage of the premium over the life of the contract. The NAIC RBC framework recognizes the margins existing in PADs via incorporation into Authorized Control Level (ACL) minimum capital requirements.

b) ***Propose inclusion of the risk mitigating benefits of the dividend margin present in Closed Block assets as buffers that can provide significant loss absorption in times of stress:***

The Standardized NPR does not address closed block assets. We reiterate our recommendation from our April 30, 2012 response to the Enhanced Prudential Standards NPR that due to structural features that are embedded in the closed block operating rules (e.g., ability and expectation to adjust the dividend and therefore reduce liabilities if asset performance is worse than expected), we encourage the Board to reflect the risk mitigating benefit of the dividend margin in the closed block as buffers that can provide significant loss absorption in times of stress.

At the point of demutualization, a mutual insurance company, which converts to a stock company, allocates a specific set of invested assets for the benefit of the affected policies, referred to as a "closed block." Consequently, policyholders' contractual rights to receive dividends that represent a share of the surplus earnings are not affected by the conversion. The assets allocated to this closed block are selected such that the future cash flows produced, together with anticipated revenues from the policies, are exactly sufficient to support obligation and liabilities related to these policies including all future guaranteed benefits, reasonable policyholder dividend expectations, and certain other costs. All cash flows arising from the closed block are exclusively committed to benefit the policyholders of the closed block as specified in pre-defined operating rules.

In setting up a closed block, insurance companies define a dividend scale based on operating experience at the point of demutualization. This dividend scale can be adjusted and even eliminated depending on actual experience relative to expected cash flow and operating earnings set out at demutualization for the closed block. The objective is to exhaust all assets when the last policy in the block terminates, while achieving a fair distribution of surplus earnings among all policyholders (i.e. avoiding a situation where relatively few last surviving policyholders receive dividends substantially disproportionate to those previously received by other policyholders in the same closed block).

APPENDIX B

Unique Risk Profile of Insurance Companies

We believe that it is beneficial to focus the Board's attention on the unique differences between the business models and risk profiles of insurance companies and the banking organizations for which the proposed standards are primarily designed. Such differences provide an overarching theme for most of the comments made in this letter and should be fully considered and factored into any standards that might be applied to insurance companies under Sections 165 and 166 of the Dodd-Frank Act.

An insurance company's liabilities are the primary determinant of its overall risk profile and drive its investment decisions, assumption of credit risk and its liquidity risk exposure. Although liabilities are also an important contributor to bank risk profiles, the linkages between asset and liability risk exposures are less integrated than is generally the case for insurance business models.

- Insurance products contract to pay benefits when an insured event occurs. As promises of indemnity or protection, products such as life insurance and annuities create insurer cash flow obligations that are generally very long term in nature – often extending 30 years or more. This liability profile is unique to the life insurance industry and represents one of the primary risks of a life insurance company. The primary risks flow out of the design and purpose of insurance products and depend on insurance-specific risks such as mortality, longevity, morbidity, loss or damage to property, casualty loss, lapse and catastrophe.

- Since insurance is a liability driven business with often long term cash flow patterns, an insurance company's investment portfolio composition and credit quality distribution is highly linked to and driven by the liability profile of its insurance products.

    - Insurance companies invest in assets to match the effective duration of liabilities. Unlike banks, which can have substantial liquidity risk, insurers generally have much less liquidity risk due to their stable portfolio of in-force insurance policies with regular premium payments and contractual features of liabilities that prohibit or limit (through surrender charges and/or tax penalties) early calls by policyholders. As a result, the liquidity risks and interest rate risks are substantively different and more controlled than those inherent in the banking business model.
    - The liability profile of an insurance company also positively impacts the credit quality of its assets. Insurers generally invest in higher quality and more diversified assets to ensure that such assets can back reserve requirements against policyholder obligations. However, due to the long duration of liabilities as well as insurance contracts that guarantee minimum benefits, insurers are exposed to market risk (interest rate and equity).

    - Furthermore, in order to mitigate foreign exchange risk, insurance companies typically invest in locally denominated assets in order to back locally denominated liabilities.

- Movement in asset values in insurance companies' balance sheet due to market movements often are accompanied by offsetting movement in the economic value of liabilities; hence, dampening the impact of asset losses on the overall financial condition of an insurer.