American Property Casualty Insurance Association

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January 22, 2020

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

RE: Proposed Regulatory Capital Rules: Risk-Based Capital Requirements for Depository Institution Holding Companies Significantly Engaged in Insurance Activities
Docket No. R-1673 and RIN 7100-AF 56

Dear Secretary Misback:

The American Property Casualty Insurance Association (APCIA) is pleased to provide comments to the Board of Governors of the Federal Reserve (the Board) regarding its proposed rule for Risk-Based Capital Requirements for Depository Institution Holding Companies Significantly Engaged in Insurance Activities. APCIA is the primary national trade association for home, auto, and business insurers. APCIA promotes and protects the viability of private competition for the benefit of consumers and insurers, with a legacy dating back 150 years. APCIA members represent all sizes, structures, and regions – protecting families, communities, and businesses in the U.S. and across the globe.

APCIA commends the Board for the extensive efforts leading to this proposal. The proposed rule is a thoughtful approach to capital requirements for insurance depository institution holding companies. It incorporates an aggregation methodology that is conceptually consistent with the Group Capital Calculation (GCC) being developed in the U.S. by the National Association of Insurance Commissioners (NAIC), and with a parallel approach that is in development at the International Association of Insurance Supervisors (IAIS).

Although this proposed rule would currently only apply to a small number of insurance savings and loan holding companies (SLHCs) subject to Board supervision (several of which are APCIA members), the Board's views on capital are widely known and respected, and can influence other domestic and international standards. For example, these views may impact opinions of other jurisdictions that are participating with Board staff in the development of the Insurance Capital Standard (ICS), and influence the development of the GCC. For those reasons, we provide comments both through the lens of how the proposal will affect insurance SLHCs, as well as through the broader lens of how it may influence other insurance group capital standards currently under development.

Aggregation Methodology

APCIA believes an aggregation approach is more pragmatic and relevant for measuring group capital than, for example, the consolidated market valuation-based ICS that has recently been approved for a five-year monitoring period by the IAIS because an aggregation method is inherently linked to existing regulatory requirements of the legal entity. Our attachments underscore APCIA's views on the superiority of an aggregation approach over the ICS.

In its Notice of Public Rulemaking, the Board also requested comments about how an aggregation-based approach would be a viable alternative to the ICS, and about criteria that should be used to assess comparability to determine whether an aggregation-based approach is outcome-equivalent to the ICS. APCIA has performed extensive research and analysis on these matters, which we have previously shared and discussed with Board staff (pertinent portions are also included in the attachment in response to the Board's questions).

With respect to comparability, recent IAIS meetings held in Abu Dhabi resulted in an agreement on a definition of "comparable outcomes" and an overarching approach to guide the development of high-level principles and criteria. The specific language appears more encouraging insofar as the prospects for a finding of comparability. The language is also quite nuanced, likely reflecting the difficult nature of the negotiations. While APCIA has provided comments on comparability in the attachment, ongoing discussions with members of Team USA and our member companies may cause APCIA's positions to evolve further.

Insurance-Centric Standard

APCIA has some concerns with the proposed rule. The Board has indicated a desire to "tailor the BBA to be an insurance-centric standard." Concurrently, however, the Board has closely tied the proposed rule to its existing banking rules. A clear example of this tension is seen in the promulgation of a BBA with a buffer; while both are stated in terms of state-based Risk-Based Capital (RBC), they are nonetheless calibrated based on banking rules. As a result, there appears to be no difference in the proposed capital requirements between the businesses of banking and insurance within an insurance depository institution holding company. APCIA questions this outcome, inasmuch as there are fundamental differences between banking and insurance that relate to their unique risks and corresponding needs for capital. For example, banks are subject to withdrawals on demand, whereas non-life insurers' obligations to policyholders and other claimants are not triggered unless and until an insured event occurs.

APCIA is concerned that a calibration driven by banking rules is overly conservative. While the Board's analysis derived a 160% ACL RBC as indicative of necessary capital requirements, this proposal significantly increased that level to 250%, in order to be conservative, but without insurance-specific data as support. Furthermore, the proposed buffer requirement would apply in a framework that would disallow prescribed or permitted practices, as well as senior debt, and would only recognize risk diversification within legal entities – but not across the group.

APCIA's more significant concern is with respect to the proposed buffer. A buffer may be appropriate for banks and other depository institutions that hold balances that are payable on demand. However, non-life insurance liabilities are only paid upon the occurrence of an insured event. Transposing a banking requirement measure into insurance terms (from percentage of risk-weighted assets to percentage of RBC) is no substitute for data-based evidence to justify the application of a buffer to an SLHC's insurance business. To the contrary, it appears that the Board backed into the proposed capital requirement, by supplementing it with a substantial safety margin to arrive at the 250% BBA component, and then almost doubling it (to 485%) solely based on the banking rule. APCIA encourages the Board to reconsider the buffer for insurance, especially with respect to application of a buffer to the insurance business of an SLHC. The necessity of any buffer for insurance business, and the level of such a buffer, should be based on insurance-specific data and experience.

APCIA has similar concerns with other provisions of the proposed rule. For example, the proposed rule includes criteria from the Board's banking rules that would disallow senior debt as Tier 2 capital, despite the fact that the international insurance community (with the Board's support as a member of "Team USA") recently approved criteria in the IAIS' Insurance Capital Standard that would allow structurally subordinated senior debt to qualify as capital for regulatory purposes, albeit as a national discretion. Moreover, despite that similar supervisory guardrails could be used by the Board for senior debt as are called for in the Notice of Public Rulemaking for surplus notes, the Board has chosen not to do so, resulting in senior debt being disallowed as a component of group regulatory capital. APCIA believes senior debt—with appropriate supervisory safeguards—should also qualify as capital.

Scope of the Group

APCIA took great interest in footnote 34 of the proposed rule, which states as follows:

> The Board recognizes that, where a firm's structure includes a number of companies that control an IDI [insured depository institution], it may be more practical and efficient, particularly in terms of reducing implementation burden, to treat, for purposes of the BBA, a mid-tier entity as the top-tier SLHC with the upstream controlling entity(ies) left outside of the BBA's scope. For instance, if an insurance institution is controlled by a company significantly engaged in non-insurance, commercial activities, it may be practical, and *without compromising the quality of the Board's consolidated supervision, to focus the BBA's application on the insurance institution rath*er than the broader commercial enterprise. (emphasis added)

In a meeting with Board staff, APCIA staff inquired as to why such language appeared as an informational footnote, but not as an actual provision in the proposed rule. Board staff responded that existing supervisory discretion already provides the ability to focus on the insurance institution rather than the broader commercial enterprise.

However, an APCIA member company was further informed by Board staff that the determination of the covered institutions for Federal supervision is made during the application process when a group requests approval to purchase a depository institution. This determination is made based on the ownership and control rules found in the Bank Holding Company Act, which are applicable to depository institutions. We understand that the Bank Holding Company Act and the control rules were updated by the Board in the spring of 2019. The updated rules apply a three-part test for determining control:

(i) the company, directly or indirectly, owns, controls, or has power to vote 25 percent or more of any class of voting securities of the bank;
(ii) the company controls in any manner the election of a majority of the directors or trustees of the bank; or
(iii) the Federal Reserve determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a "controlling influence" over the management or policies of the bank.

Based on these criteria, it appears that supervisory discretion is exceedingly limited. Accordingly, APCIA requests the Board to consider language in the proposed rule itself (rather than a footnote) that would extend and clarify the discretion available to the Board to focus the BBA's application on the insurance institution rather than the broader commercial enterprise.

Section 171 Calculation

APCIA believes that a separate Section 171 calculation is not necessary. Section 171 of the Dodd-Frank Act generally requires the Board to establish minimum risk-based capital requirements, on a consolidated basis, that are at least as stringent as the generally applicable capital requirements for insured depository institutions. The BBA itself meets those conditions. Therefore, APCIA recommends the BBA itself be used to document compliance with Section 171, thus allowing the Board and SLHCs alike to forego the additional and unnecessary burden that would be incurred in calculating and applying supervisory analysis and measures to a separate metric.

* * *

Detailed responses to many of the questions posed by the Board in the Notice of Public Rulemaking are contained in the first attachment. APCIA appreciates the extensive work of the Board in developing the proposed rule, and of the Board's staff in being accessible and open to discussion with APCIA and its members. APCIA stands ready to discuss this letter and our responses to the Board's questions about the proposed rule at your convenience.

Sincerely,

Phillip L. Carson
Department Vice President, Financial Regulation

Stephen W. Broadie
Vice President, Financial & Counsel

Responses to the Questions Posed by the Board

Question 1: The IAIS is currently considering a MAV approach for the ICS; in contrast, the BBA aggregates existing company-level capital requirements throughout an organization to assess capital adequacy at various levels of the organization, including at the enterprise level. What are the comparative strengths and weaknesses of the proposed approaches? How might an aggregation-based approach better reflect the risks and economics of the insurance business in the U.S.?

This question strikes at the heart of an issue that has united APCIA's members around a policy position that is key to APCIA's ongoing advocacy involving international standard-setting: the consolidated, MAV-based ICS is unsuitable for its intended purpose and has numerous disadvantages as compared to an aggregation approach. The relative strengths and weaknesses of each have been presented in written testimony (see Attachment 2) of APCIA President and CEO David A. Sampson to the Senate Banking Committee for its September 12, 2019 hearing on "Developments in Global Insurance Regulatory and Supervisory Forums." APCIA's research in this area has also been presented and discussed with Board staff, the key points being as follows:

1. A MAV-based ICS is Inconsistent with Societal Needs for Insurance in the U.S.
    - The demand for insurance products and services is an inherently local phenomenon.
    - Private versus public sector involvement in insurance is embedded in overarching government policies and reflects each nation's unique history and broader socio-economic developments.
        - Examples: taxation and state/federal budgets, national versus state and local authority, economic development, retirement and pension funding, disaster/ catastrophe recovery and loss mitigation, policyholder protection schemes, mortgage financing, credit protection, and more.
    - Jurisdictions simply differ in these matters; they cannot be changed by the supervisor, nor can they be reflected in a single, unadaptable capital standard.
    - The U.S. has, and will, for the foreseeable future, lean toward private (rather than public) involvement in these matters; the system of insurance supervision in the U.S. recognizes that reality.
    - The ICS is heavily skewed toward the societal aspects of other parts of the globe; it may work very well for the more basic products and business models in those jurisdictions, but not for the full spectrum of needs in the well-developed U.S. market.
    - Implementing ICS 2.0 in the U.S. would have a significant negative impact on the availability and affordability of key products which U.S. consumers need and which, for the U.S., the private sector must supply.
        - The state-based system relies on statutory accounting, risk-based capital, and other tools that have shown prudence while accommodating U.S. needs for insurance products and services.
        - An aggregation-based group capital metric incorporates and builds on those tools, is consistent with U.S. societal needs, assures policyholder protection, and contributes to financial stability.

2. The ICS Will Not Work for the U.S. – Technical Issues

    - The MAV-based ICS is not aligned with the well-developed existing supervisory system, processes, and tools used in the state-based system, and it would:
        - Be a one-off signal from all other aspects of that system;
        - Not be actionable by state supervisors who need to know how group-wide risks impact legal entity insurers within the group to utilize indirect powers over unregulated entities; and
        - Conflict with the metrics that U.S. firms use to manage their business.
    - The ICS would thus:
        - Introduce significant risk into supervisory decision-making processes;
        - Detract management's focus as they calculate, rationalize, and explain a one-off metric to supervisors, rating agencies, and other stakeholders; and
        - Impose high (and unnecessary) implementation costs.

3. The ICS is Not Conducive to Established Assurance Measures

    - U.S. statutory accounting and U.S. GAAP are promulgated by supervisors and accounting standard setters, respectively, and subject to supervisory exams and independent audit.
    - The ICS is not based on audited data; it could be, but not without significant costs.
    - The one-off nature of the ICS relative to other U.S. regulatory tools presents concerns:
        - There is no ready means to independently assess if an IAIG's ICS ratio has been misstated – other than through a complete recalculation from the ground up.
        - There are no metrics or sources to compare to a group's ICS to assess its reasonableness.
    - There is an inherently high risk of misstatement (and misinterpretation) of a MAV-based ICS.

4. The ICS is Fundamentally Flawed for the U.S.

    - The ICS purports to be a going concern measure but is, illogically, MAV-based:
        - MAV assumes temporary market movements are effectively realized, which will produce spurious volatility and procyclicality contributing to herding behavior.
        - Risks underwritten by life insurers are long-term in nature and supported by liability-driven investing; non-life cash outflows are driven by insured events (which are not correlated to macroeconomic factors) and are not payable on demand.
    - The ICS inherently (and unrealistically) assumes that trapped capital in legal entities is fungible across the group and all the jurisdictions in which it operates.
    - The ICS ignores frictional costs of having to move capital, including but not limited to tax-related implications (including different tax rates) at jurisdictional and legal entity levels.
    - The IAIS will not commit to an ongoing effort during the monitoring period sufficient to provide confidence to field-test firms and stakeholders that all remaining issues will be identified and resolved satisfactorily.

- The ICS thus poses risk to the sector as a stabilizer during periods of stress or market turmoil; its ability to prudently manage risks underwritten based on product economics; and its ability to play a leading role in supporting jurisdictional social, public, and economic policy initiatives.

5. An Aggregation Method is Best for the U.S. because it:
    - Avoids the risks and costs that are inherent with a one-off market-based metric.
    - Is an incremental and pragmatic natural extension of the existing state-based system.
    - Is aligned with all aspects of that system (which has been shown to be effective).
    - Is aligned with other financial reporting metrics and tools used by insurers and insurance groups in the U.S.
    - Is more easily understood, aligned with legal entity requirements, and based on audited data.
    - Promotes confidence in supervisory colleges since participants can readily see how data from a group's entities in each jurisdiction is input and aggregated.
    - Is transparent, i.e., displayed in sub-group ratios, by jurisdiction or business unit, to allow a better understanding of the sources and risks to group capital, including with respect to fungibility.

APCIA asserts that an aggregation approach better reflects (than the MAV-based ICS) the risks and economics of the insurance business in the U.S. because it is based on risk charges that benefit from decades of experience across the entire population of regulated insurers, which have been determined and applied at a more granular level by type or line of business.

Those who endorse a MAV-based approach point to its transparency in reflecting risk, i.e., an event occurs, is seen in changed market values, and can then be instantly quantified and measured. This is likely an overly simplistic explanation that may not work well in the real insurance world. MAV depends on a contrived approach to the determination of estimated market values for insurance liabilities, which are not subject to market trades. Even on the asset side of the balance sheet, some assets are not traded, so market-value estimates are based on models which could introduce modeling risks. Finally, even if short-term market movements could somehow be measured reliably and accurately, the resulting measure might not provide the entire understanding and management of the economics of a business that is not subject to payments on demand and for which assets, liabilities, and corresponding cash flows are managed over many years and business cycles. In short, MAV may drive volatility in results that company managers and supervisors alike would then spend time explaining away, so they could then try to identify and focus on what all that volatility is masking – emerging risks, longer term trends, and their drivers.

Question 2: In what ways would an aggregation-based approach be a viable alternative to the ICS? What criteria should be used to assess comparability to determine whether an aggregation-based approach is outcome-equivalent to the ICS?

As to how an aggregation-based approach could be a viable alternative to the ICS, we refer to our response to Question 1 and, in particular, the point raised in item 5, describing why an aggregation method is best for the U.S. because this approach:

- Avoids the risks and costs that are inherent with a one-off market-based metric.
- Is an incremental and pragmatic natural extension of the existing state-based system.
- Is aligned with all aspects of that system (which has been shown to be effective).
- Is aligned with other financial reporting metrics and tools used by insurers and insurance groups in the U.S.
- Is more easily understood, aligned with legal entity requirements, and based on audited data.
- Promotes confidence in supervisory colleges since participants can readily see how data from a group's entities in each jurisdiction is input and aggregated.
- Is transparent, i.e., displayed in sub-group ratios, by jurisdiction or business unit, to allow a better understanding of the sources and risks to group capital, including with respect to fungibility.

Regarding criteria to determine comparability of an aggregation approach to the ICS, that too continues to be discussed within APCIA, as well as with the other members of Team USA. To some extent, the IAIS senior committee meetings in Abu Dhabi late last year laid the groundwork for comparability (in what is referred to herein as the "AD Agreement"), alleviating some of the very difficult challenges that had previously been enshrined in the KL (Kuala Lumpur) Agreement. Notable in the AD Agreement – subject to further IAIS negotiations and stakeholder consultation – is the definition of "comparable outcomes". In that regard, the AD Agreement states as follows:

- "The IAIS aims to be in a position by the end of the monitoring period to assess whether the AM provides comparable (ie substantially the same (in the sense of the ultimate goal)), outcomes to the ICS. If so, it will be considered an outcome-equivalent approach for implementation of ICS as a PCR."
- "Comparable outcomes to the ICS means that the Aggregation Method (AM) would produce similar, but not necessarily identical, results over time that trigger supervisory action on group capital adequacy grounds."

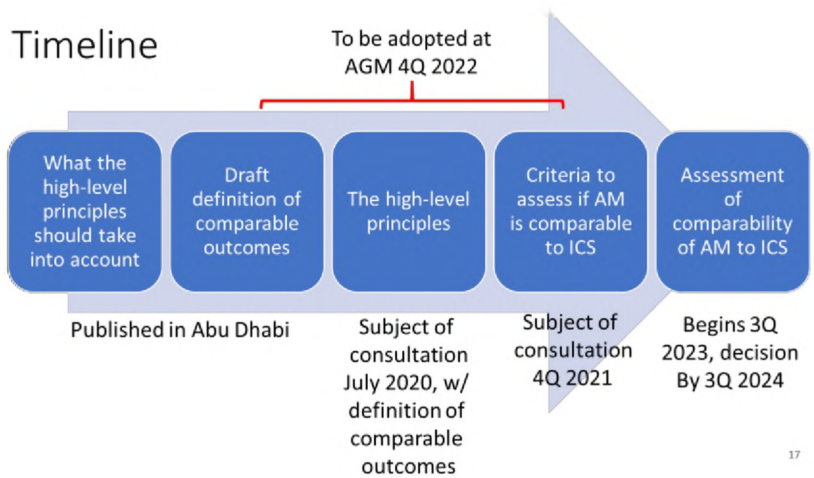
The first point above is consistent with the KL Agreement from two years earlier. Unfortunately, it continues to misuse the spirit of the "ultimate goal", which was agreed to in 2015 by the IAIS. As stated then, the ultimate goal was an aspiration to which no deadline was attached. However, that language was pulled into the KL Agreement and assigned a date certain by which it was to be achieved in the sense of comparability of AM to the ICS – or else. And, as seen above, the same thought has been maintained in the AD Agreement.

However, the second point cited above from the AD Agreement does put that in a somewhat different context with an agreed definition of "comparable outcomes". The definition is explicit in the expectation that comparable does not mean "identical". Instead, comparable means "similar", and similarity is to be gauged not at a point in time, but over a span of time. The key attribute is the triggering of supervisory action (i.e., a point of intervention) – and not what those supervisory actions might actually be.

While there remains some nuances in the verbiage that we are sure will continue to be the source of some debate at the IAIS, the agreed definition of "comparable outcomes" is a positive development and incorporates concepts that APCIA had been advocating for some time (i.e., that the KL Agreement had installed an "identical standard" that, at the outset, could never have been seen as achievable; that at any point in time the two methods being compared would inherently differ, by amounts and directions which would also differ over time, perhaps significantly; and that the only rational aspect that can actually be compared is the point of intervention, and not the nature of that intervention). APCIA would have preferred more clarity about those points in the agreed definition, but understands the practical challenges involved in any difficult negotiation.

The publication of the Board's NPR and its question about what the criteria should be to assess comparability predated the AD Agreement, which put forth a high-level framework purportedly designed to lay the groundwork to determine such criteria and, ultimately, to apply that criteria in arriving at a determination by the end of the Monitoring Period as to whether the AM is, or is not, comparable to the ICS. To that end, the AD Agreement states that the IAIS "agreed on the definition of comparable outcomes and an overarching approach to guide the development of high-level principles and criteria." The related timeline calls for a public consultation on the high-level principles to be published July 2020, and another consultation on the draft criteria to be published during the fourth quarter of 2021. Therefore, it seems that more time is available to consider comparability criteria than the Board may have earlier considered when it published the NPR.

An illustration of the overall approach and timeline put forth by the IAIS in Abu Dhabi is as follows:



Thus, while we appreciate the Board's current interest about the insights of stakeholders on comparability criteria, APCIA's own views will evolve over time, in particular as the IAIS publishes in July its consultation on the draft definition of "comparable outcomes" and the high-level principles, and again in late 2021 when it publishes its consultation on the criteria. APCIA is not waiting for those publications, however, and is actively working with members to gather and refine views on those points for purposes of sharing with Team USA as its members go into negotiations over the drafting of the IAIS consultation documents.

Question 6: What other calculations, if any, should the Board consider to ensure that the minimum risk-based capital requirement for insurance depository institution holding companies complies with section 171 of the Dodd-Frank Act?

APCIA believes that a separate Section 171 calculation is not necessary. Section 171 of the Dodd-Frank Act requires the Board to establish minimum risk-based capital requirements, on a consolidated basis, that are at least as stringent as the generally applicable capital requirements for insured depository institutions. The BBA itself meets those conditions. As the Board explicitly recognizes in the proposed rule, "the BBA framework was designed to produce a consolidated risk-based capital requirement that is not less stringent than the results derived from the Board's banking capital rule." Based on the Board's own analysis, the BBA itself is sufficient to meet the requirements of Section 171 of the Dodd-Frank Act.

Further, Section 171(c) provides that the Board is not required to include for any purpose of Section 171 (including in any determination of consolidation) any entity regulated by a state insurance regulator. Although Section 171(c) provides the Board an option to exclude insurance companies from Section 171, there is no requirement for the Board to do so. Accordingly, a separate Section 171 calculation, in conjunction with the BBA, is not necessary.

APCIA recommends the BBA itself be used to document compliance with Section 171. This will allow the Board and SLHCs alike to forego the additional and unnecessary burden that would be incurred in calculating and applying supervisory analysis and measures to a separate metric.

Question 14: What other definitions of materiality, if any, should the Board consider for use in the BBA? Examples may include a threshold based on size, off-balance sheet exposure, or activities including derivatives or securitizations.

APCIA considers that there are several aspects to the question: whether quantitative or qualitative factors, or both, are considered; the base upon which materiality is measured (equity, surplus, risk exposure, etc.); and the specific measure applied to that base which would trigger a determination of materiality (e.g., 1%, 5%, etc.). The NPR includes both quantitative and qualitative factors, either of which taken separately could result in a finding that an entity is material.

The quantitative base that is used is total assets. APCIA understands that was based on a consideration of banking capital rules, with some adjustment. However, we note that using total assets as a base seems unusual compared to other settings where materiality determinations are made. For state-based regulation, surplus (statutory-basis equity) is typically used. Independent auditors of U.S. GAAP-basis financial statements consider equity as well as the impact of potential misstatements on earnings and earnings trends. Using total assets can be potentially discriminatory based on the line or sector of business. Life insurers accumulate and invest large amounts over many years, and thus have a much higher asset base than, for example, many non-life insurers or health insurers. As a result, a quantitative measure based on total assets would be higher and thus less likely to trigger a materiality determination of a non-insurance entity in a life group, as compared to a non-life or health group. APCIA suggests that the Board consider measures based on surplus or equity, which would result in less disparate treatment across sectors.

As to a quantitative threshold, a 1% threshold seems too low. A non-insurance entity that exceeds the 1% threshold would have to be parsed out as an MFE and subjected to bank capital rules. This can produce anomalous results where the subject entity is nonetheless an integral part of the overall insurance business segment and subjected to capital management on that basis. It can also increase the overall burden in complying with the BBA.

Question 15: What thresholds, other than the proposed threshold for exposure as a percentage of total assets, should the Board consider for use in the BBA's definition of materiality? What are advantages and disadvantages of using a threshold based on the top-tier depository institution holding company's building block capital requirement?

Please see APCIA's response to Q14.

Question 22: The Board invites comment on the proposed approach to scalars and the associated white paper. What are the advantages and disadvantages of the approach? What is the burden associated with the proposed approach?

APCIA views that the scaling approach is thoughtful and technically researched. However, we observe that there are potential issues around the definition of default and related implications as to which entities/situations meet that definition, and then, whether there is an appropriate data source to identify them. For example, there are companies that just stop writing business and go into runoff, and which do not enter any proceedings; are these identified?

Inasmuch as the current population of SLHCs significantly engaged in insurance writes virtually no business outside the U.S., the only scalars that were developed are between U.S. banks and U.S. insurers. Should the need arise in the future for scaling between insurers in non-U.S. jurisdictions, the Board's approach to scaling in the white paper may not be feasible given limits on available data. Thus, the concepts put forth in the white paper methodology may take on added credibility if adopted for the BBA, but they would be of little practical use if situations calling for scaling among jurisdictions were to arise.

The Board does have a "provisional approach," should the need arise for an international scalar, one criterion being that the jurisdiction is in a "scalar compatible framework." However, "provisional" implies a temporary application, presumably while more appropriate scalars could be developed. And where the jurisdiction is not in such a framework, U.S. capital rules would apply. That seems to suggest applying RBC, which would be challenging given differences in valuation and lack of comparable information to include in an RBC template.

Question 23: How should the Board develop scalars for international insurance capital frameworks if needed?

APCIA encourages the Board to continue to work with the NAIC and state insurance regulators as they develop international scalars for the AM and GCC and, to the maximum extent possible, to conform any international scalars it may use to those.

Question 26: What other criteria, if any, should the Board consider for determining available capital under the BBA?

APCIA understands that in developing the BBA, the Board sought to tailor it "to be an insurance-centric standard" while at the same time recognizing that the Board has already established precedent in some similar areas with respect to other regulated institutions (i.e., other than SLHCs significantly engaged in insurance activities). The tension between those two objectives can be seen with respect to the divergent approaches to the NPR for available capital and, specifically, the criteria for capital instruments. In that regard, comparing and contrasting the NPR's approach for surplus notes and for senior debt is instructive.

Under U.S. GAAP, both surplus notes and senior debt are liabilities, i.e., they represent amounts that have been borrowed and which are to be repaid to a lender. Insurance supervisors have nonetheless allowed insurers to report them as components of capital for supervisory purposes under certain circumstances, the most important of which are that the instruments be effectively subordinated to policyholders and that amounts to repay principal and interest be subject to supervisory approval.

APCIA understands that the primary concern of the Board, as reflected in the proposed criteria, is that calls and redemptions of surplus notes, while subject to approval of a state regulator, are not subject to approval by a federal regulator, such as the Board. The NPR proposes to grandfather in existing surplus notes, but new notes must comply with the criteria, which presumably would qualify a new surplus note as capital only if it required dual sign-offs of calls and redemptions, i.e., by a state supervisor as well as the Board itself. That appears to be a reasonable approach, assuming neither supervisor's approval is unreasonably withheld.

However, with respect to senior debt, there are other criteria that would preclude capital treatment. APCIA has been informed by Board staff that this is primarily related to precedent in the banking rule, for which the Board felt compelled to make consistent across SLHCs, whether or not significantly engaged in insurance activities.

Nonetheless, APCIA considers it anomalous that senior debt and surplus notes be treated differently. Both are debt for GAAP, and both are subordinated to policyholders. Perhaps the primary difference is that the Board will review and, if appropriate, approve calls and redemptions of surplus notes, whereas it does not propose to do so or provide similar supervisory guardrails (in the NPR) with respect to senior debt. The difference in treatment also highlights a departure from the manner in which supervisors in other jurisdictions evaluate and qualify debt for capital treatment, and a departure with international standards. Recently, in Abu Dhabi, the IAIS agreed to criteria that a jurisdiction could use as a "national discretion" in its implementation of the ICS that would allow structurally subordinated senior debt to qualify (existing ICS criteria already can qualify contractually subordinated debt).

While APCIA appreciates that there is precedent for treatment of senior debt in the banking rule, such treatment did not benefit at the time from any considerations involving the supervision of insurers. Given the anomalistic and divergent treatment between surplus notes and senior debt in the NPR, APCIA believes the proposed treatment of senior debt should be revisited by the Board and made more consistent with emerging international standards.

Question 30: What alternate formulations of the limit on tier 2 capital may be more appropriate, while still ensuring appropriate quality of capital?

APCIA's understanding is that, for the BBA, no more than 62.5% of the building block capital requirement for the top-tier parent can be comprised of Tier 2 resources, a provision intended to assure that the BBA is no less stringent than corresponding banking requirements of 6% of risk-weighted assets. With respect to the buffer, it cannot be backed by any Tier 2 resources. Thus, only 25% of the capital resources held to meet the enterprise-wide BBA requirement may be Tier 2 resources (62.5%/250%), and only 12.9% of the capital resources held to meet the combined BBA and buffer requirement may be Tier 2 resources (62.5%/485%).

By comparison, APCIA has referred to the capital limits for the ICS. Such limits that would apply to ICS 2.0 for the monitoring period were not detailed in the "Level 1" document published after the Abu Dhabi meetings, and will not be available until a "Level 2" document is published next spring. However, the Technical Specifications for 2019 field testing of the ICS provide that Tier 2 capital resources were limited to 50% of the ICS capital requirement.

Without further information from the Abu Dhabi meetings, for purposes of this APCIA response it is assumed that the 50% limit will be retained by the IAIS for the monitoring period. If so, there is a material difference between the 50% for Tier 2 in the ICS and 12.9% as determined by the Board for the combined BBA and buffer. APCIA's view is that such a large difference is difficult to comprehend and results primarily from the application by the Board of the buffer and its level of calibration (please see APCIA's response to Question 33).

Question 32: The Board invites comment on the proposed minimum capital requirement. What are the advantages and disadvantages of the approach? What is the burden associated with the proposed approach?

APCIA observes that the design of the BBA to determine an insurance depository institution holding company's (IDIHC) capital ratio is based on existing jurisdictional requirements, e.g., RBC in the case of U.S.-based insurance entities or, for banking operations, banking measures scaled to RBC. In that respect, it is insurance centric and addresses a major concern of insurers when the Board adopted capital requirements in 2013 which, due to their bank-centric nature, exempted IDIHCs.

However, the calibration of the resulting capital requirements is based on the Board's rules applicable to banking. Stated differently, and notwithstanding the proposed insurance-specific rule, IDIHCs would wind up with a quantified capital requirement like that which would apply if they were subject to banking rules; it is just stated in insurance terms (RBC) rather than banking terms (risk-weighted assets). Moreover, it would appear that the BBA (excluding the buffer) is actually more conservative than the stated 250% ACL RBC level would imply, in that it also is based on the non-inclusion of senior debt as a capital resource, the unwinding of prescribed and permitted practices, and lacks diversification credit across legal entities. Including the buffer to reach a total requirement of 485% ACL RBC yields a threshold that is higher than the held RBC of some well-recognized and rated non-life insurers, suggesting that a single measure to be used regardless of business sector is not appropriate.

Nonetheless, for the BBA component (which excludes the buffer, which is another matter – please see APCIA's response to Q33 for comments on the buffer), the resulting calibration approximates existing state-based insurance requirements. It is also based on an aggregation method, which is fundamentally more practical to implement than, for example, a consolidated approach such as the ICS that has no linkage to existing regulatory requirements. APCIA therefore considers that, in those respects, the incremental burden associated with the BBA component would be minimal.

However, APCIA also notes that there are some details within the BBA that can be unduly burdensome depending on the facts and circumstances of a specific SLHC. For example, the possible need to "unwind" transactions with reinsurance captives, to restate balances to nullify the impact of prescribed or permitted transactions or, for life insurers, to apply PBR retroactively.

Question 33: The Board invites comment on the proposed minimum capital buffer. What are the advantages and disadvantages of the buffer? What is the burden associated with the buffer?

APCIA understands that, in developing the BBA, the Board sought to tailor it "to be an insurance-centric standard" while at the same time recognizing that the Board has already established precedent in some similar areas with respect to other regulated institutions (i.e., other than SLHCs significantly engaged in insurance activities). While there would be some obvious tension in balancing the focus on those two different objectives, in the case of the buffer, the Board seems to have come down on one to the exclusion of the other. Although stated in terms of RBC (235%) and thus the appearance of being insurance-based, the buffer fundamentally is a banking rule that is nonetheless to be imposed on insurance SLHCs. Thus, unlike the BBA component for which APCIA's concerns are more focused on the degree of calibration (see response to Q32), APCIA has more significant concerns with respect to the buffer.

The Board certainly has experience with the need for a buffer and its calibration and application to banks and other depository institutions. However, the business of insurance is considerably different in many respects, especially in that policyholder benefits are not payable upon demand. That is especially true for non-life lines, for which benefits are only paid upon the occurrence of an insured event. It appears that, other than transposing a banking requirement measure into insurance terms (from percentage of risk-weighted assets to percentage of RBC), the Board has not presented evidence of a need for such a buffer for application to an SLHC's insurance business. To the contrary, it appears that the Board determined an appropriate capital requirement, supplemented that with a substantial safety margin to arrive at the 250% BBA component, and then almost doubled that (to 485%) solely based on the banking rule.

While the BBA and the buffer have limited application to what is currently a small number of insurance SLHCs subject to Board supervision, the Board's views on capital are widely known and respected, and can have influence that may go well beyond that limited group. For example, they may impact the views of other jurisdictions who are participating with Board staff at the IAIS in the development of the ICS. APCIA encourages the Board to reconsider the buffer, especially with respect to application to the insurance business of an SLHC, and to base the determination on whether insurance data and experience shows a need for a buffer.

Question 36: The Board invites comment on all aspects of the foregoing evaluation of the potential impacts of the proposed rule. Are there additional impacts that the Board should consider? Would the magnitude of any impact be different than as described above?

The Board's proposed rule may have potential impacts that can go beyond the Board's regulatory objectives with respect to insurance SLHCs. Those objectives are focused on protecting the safety and soundness of the depository institution within the group. In its efforts to attain those objectives in the proposed rule, the Board has sought an "insurance-centric" approach, but also has largely kept to provisions that would be consistent with banking rules. As a result, there appears to be no difference in the proposed capital requirements between the businesses of banking and insurance within a SLHC. We see this result in the BBA and the buffer; while both are stated in terms of RBC, they are nonetheless calibrated based on banking rules. Even if the Board in its final rule finds that such banking measures are appropriate for depository institution holding companies that are significantly engaged in insurance, APCIA considers that they are not appropriate for other U.S. insurance groups, for which the primary objective of state-based regulation is the protection of policyholders.

The Board is an integral component of Team USA and is actively engaged at the IAIS and with other jurisdictions in the development of international insurance supervisory standards, including the ICS. The Board has considerable respect and stature within the international regulatory and supervisory community. As a result, IAIS members from other jurisdictions may look to the proposed rule as evidence or support of a need for a calibration level or some other features (e.g., disallowance of senior debt as a capital resource) in the ICS like those in the BBA. To the extent that such banking-like features are retained in the final rule, it is imperative that the Board, and Team USA as a whole, make sure that other IAIS members are aware of the Board's unique objectives with respect to SLHCs and are discouraged from considering that such calibration levels/features would be appropriate in the ICS.

American Property Casualty Insurance Association

INSURING AMERICA apci.org

STATEMENT BY DAVID A. SAMPSON, PRESIDENT AND CEO, FOR SEPTEMBER 12, 2019 HEARING OF SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

The American Property Casualty Insurance Association (APCIA) thanks the Committee for holding this very timely and important hearing on "Developments in Global Insurance Regulatory and Supervisory Forums." APCIA is the primary national trade association for home, auto, and business insurers. APCIA promotes and protects the viability of private competition for the benefit of consumers and insurers, with a legacy dating back 150 years. APCIA members represent all sizes, structures, and regions – protecting families, communities, and businesses in the U.S. and across the globe.

APCIA is deeply concerned that the International Association of Insurance Supervisors (IAIS) will adopt an international capital standard that is unfit for purpose and potentially harmful to U.S, insurance groups, despite continued objections by U.S. state insurance regulators as represented by the National Association of Insurance Commissioners (NAIC), the Federal Reserve Board (FRB), and the Federal Insurance Office (FIO) of the U.S. Department of Treasury (collectively, "Team USA"). Guarding against this threat is precisely the purpose of the Heller-Tester International Insurance Capital Standards Accountability Act that Congress enacted last year. APCIA asks for continued strong Congressional involvement and support for our Team USA representatives as they engage with their international counterparts and urge a broader perspective that includes valid and robust alternative approaches to capital assessment.

The U.S. has the largest and most diverse insurance market in the world, with a 150-year track record of comprehensive state solvency regulation protecting consumers. The U.S. property casualty industry has played a major role in helping to bring about safer homes, workplaces, and highways through efforts that have saved countless lives and preserved important resources. Over the last three years, United States consumers suffered record losses from historic natural disasters – hurricanes, wildfires, earthquakes, and tornadoes. The insurance industry rose to the challenge, communicating closely with policyholders, working with federal and state disaster crews and regulators, and speeding claims payments to families and businesses suffering losses. Despite these tremendous challenges, U.S. industry solvency and financial strength have remained at record highs.

Although the capital standards of the U.S. insurance regulatory system have served the U.S. well, the IAIS continues to push for global approval of its proposed Insurance Capital Standard (ICS), which is not yet fit for purpose and is inconsistent with the U.S. insurance regulatory system. The IAIS currently intends at its November 2019 meeting in Abu Dhabi to force approval of its latest version of the ICS for a final monitoring period and subsequent implementation. U.S. regulators – the FRB and the individual state insurance regulators – have unequivocally stated that the ICS, as currently proposed, will not be adopted as part of the U.S. insurance regulatory system. Without significant revisions, however, the proposed ICS could potentially create competitive imbalances and discriminate against U.S. insurers if widely implemented in other jurisdictions.

<u>The ICS is currently "unfit for purpose."</u>

The current version of the ICS is "unfit for purpose" for many reasons, including the following:

- the approach does not identify where capital weaknesses and available capital exist within a group (by entity or jurisdiction);
- there is no recognition of the restraints or costs related to moving capital within a group;
- regulators would need authority that extends beyond their home jurisdictions to apply the ICS, *i.e.*, the requirement is extra-territorial; and
- the valuations used in the standards under the market-adjusted valuation (MAV) approach are unaudited.

There are inherent difficulties in trying to draft a single global insurance capital standard. Perhaps the most pervasive of these problems involves differences in the needs and demand for private-sector insurance products and services across jurisdictions. Such needs are founded in differences in core jurisdictional-specific aspects such as legal structures, and national policies involving taxation, catastrophe recovery, policyholder protection systems, private vs. public sector funding and involvement, and a myriad of other issues that make it impossible for one global capital system to appropriately capture these inter-jurisdictional differences in a consolidated approach.

Rather than attempting to develop a system that builds upon and complements current, well-established regulatory systems, the IAIS decided to develop a one-size-fits-all global group standard modeled after the nascent European banking-style Solvency II regulatory system. As a result, the ICS produces a single group ratio that does not provide sufficient information on how group-wide risks impact the legal entity insurers within the group.

The ICS is intended to be a group indicator of capital adequacy, applicable to Internationally Active Insurance Groups (IAIGs). The ICS will be part of another IAIS supervisory product, referred to as the "Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame)." As the ICS has evolved from the ComFrame context in which it was created, it has become heavily skewed towards the banking/Solvency II approach. Indeed, the ICS imposes group capital requirements that are fundamentally inconsistent with the more extensive group supervision approach adopted by the United States and other jurisdictions.

Additional challenges in establishing a global capital standard arise due to jurisdictional differences in accounting and valuation standards. U.S. statutory accounting principles (SAP) and generally accepted accounting principles (GAAP) require valuation of property-casualty claim and expense liabilities at management's best estimate of their undiscounted ultimate cost, which is subject to an independent audit and can be back-tested. The current ICS proposal bases insurance liabilities on market-adjusted valuation (MAV), discounting insurance liabilities to present value and then adding a risk margin for the uncertainty in the expected liability – measures which preclude back-testing and therefore diminish reliability.

Under the MAV-based ICS proposal, short-term movements in market value create artificial and excessive volatility in capital requirements, even though the amount and timing of policyholder benefit and claim payments are unaffected by such market movements. The ICS proposal incorrectly assumes that the insurance group's capital, which may be domiciled in different states or countries, is fungible within the group, even in times of stress and across jurisdictions, without acknowledging the costs (including impact on policyholder protection) associated with moving that capital. In addition, the ICS does not recognize all material sources of capital typically available to U.S.-based insurance groups.

Lastly, the ICS proposal would be an inefficient approach to providing a global capital standard as it would require a global body to maintain the relevancy of risk factors for the products written throughout all the jurisdictions of the world even as new products arise and risks evolve in various regions/countries. In contrast, an aggregation approach leverages the work of local regulators to keep their capital standards relevant. The incentive and closeness to local risks makes local regulators more qualified for the task of keeping capital standards appropriate to their respective jurisdictions than a centralized global body.

Thus, APCIA is concerned that the combined impact of the above-mentioned adverse capital consequences of the MAV-based ICS proposal could negatively impact the availability and affordability of long-term insurance and retirement security products, as well as certain other property-casualty products, while also imposing significant implementation and ongoing maintenance costs on regulators and the U.S. industry. In brief, implementation of the ICS into the U.S. state-based regulatory system creates the potential to do more harm than good for the protection of U.S. policyholders.

Team USA and U.S. stakeholders strongly oppose the ICS.

Leadership at each of the Team USA constituent bodies have objected to the application of the ICS to the U.S. insurance marketplace. In addition, U.S. Treasury Secretary Steven Mnuchin stated at the May 2019 NAIC International Forum that if "these standards are adopted by foreign jurisdictions, they could have significant implications for U.S. insurers operating overseas, and potentially for our domestic insurance sector and regulatory regime" (https://home.treasury.gov/news/press-releases/sm688). Secretary Mnuchin criticized the "ICS's market valuation approach and the negative effects it could have on the ability of insurance companies to provide long-term savings products, which are important to insurers and policyholders in the United States." Mnuchin suggested that, instead of racing to meet a "fixed schedule that mandates completion of the ICS at a specific point in time," the IAIS should "recognize and accommodate the diverse approaches to solvency regulation taken by various jurisdictions around the world, including our U.S. state-based regulatory system", and specifically recognize the U.S. aggregation approach to group capital as "outcome equivalent" to the ICS.

In January, FRB Vice Chairman for Supervision Randal Quarles stated that, "the ICS would face implementation challenges in the United States. For instance, such a framework may fail to adequately account for U.S. accounting frameworks, both Generally Accepted Accounting Principles (GAAP) and the NAIC's Statutory Accounting Principles, introduce excessive volatility, and involve excessive reliance on supervised firms' internal models." (https://www.federalreserve.gov/newsevents/speech/quarles20190109a.htm) Vice Chairman Quarles further stated that a "capital standard that uses market-based valuation can introduce volatility and procyclicality, and one that is excessively volatile or procyclical can influence a firm to veer away from a long-term perspective and concentrate instead on the short term. This can have undesirable consequences, including diminishing product availability."

At the May 2019 NAIC International Forum, the President of the NAIC, Maine Superintendent of Insurance Eric Cioppa, stated that the ICS "car is still missing two wheels." Cioppa specified that:

- The ICS is currently not fit for purpose; with many believing that no number of technical tweaks can address the fatal design flaws within the ICS.
- Alternatives to the ICS need to be recognized, such as an aggregation method.
- As currently designed, the ICS will negatively impact the ability of insurers to offer long-term products and make long-term investments.
- The idea of the ICS providing a "level playing field" is unrealistic and unnecessary for assessing an [internationally active insurance group's] group capital position, nor is it reflective of the strength of any particular supervisory approach.
- The assessment of comparable outcomes needs to focus on qualitative elements and the overarching objective, not simply a quantitative exercise that compares one number to another. (https://www.naic.org/documents/190513_speech_2019_forum_cioppa.htm)

U.S. insurance supervisors are building a better approach that should be equally recognized.

The states and the FRB are developing aggregation-based group capital assessment systems that promise to be a better fit for the U.S. market and regulatory system than the ICS in addition to being much more susceptible to ongoing maintenance and continued relevancy. Both the states and the FRB are building upon the current U.S. legal entity solvency regulation regime and accounting systems to develop this approach. The aggregation methodology leverages the existing legal-entity regulatory approach in the U.S. to allow both a legal entity/jurisdictional view, as well as a combined view, of an insurance group's capital.

The NAIC's Group Capital Calculation initiative (GCC) and the FRB's parallel Building Block Approach (BBA) are both based upon aggregation of current insurance *company* capital resources and capital requirements, using the long-established state risk-based capital (RBC) system and, where applicable, corresponding existing requirements for non-U.S. subsidiaries of a U.S.-based insurance group. These approaches would require significantly reduced transition costs since they are based on current accounting and capital requirements. Because the GCC and BBA require aggregation of legal entity information (rather than the ICS' consolidated, top-down approach), they will be more transparent in that regulators will know both the location and availability of capital *within* legal entities of the group (which is not a feature of the ICS). The aggregation methodology uses audited data (which the ICS does not), can be applied by any home jurisdiction (and a number of other jurisdictions are interested in using an aggregation method), and provides a pragmatic incremental way forward for the U.S. to achieve the IAIS' stated goals for the ICS without compromising the current accounting and regulatory framework. The aggregation methodology also addresses the issue of capital fungibility, which is a fatal flaw in the ICS approach.

Team USA should continue to advocate for recognition of the U.S. aggregation approach as outcome-equivalent to the ICS.

APCIA and the vast majority of the U.S. insurance marketplace share the concerns of our U.S. state and federal Team USA insurance leaders. To avoid these adverse consequences, recognition and acceptance by the IAIS of the evolving U.S. domestic aggregation-based approach to group capital assessment is essential. As noted, an aggregation methodology leverages the existing regulatory system to provide solvency information from the perspective of the entity, the group, and jurisdiction. Before acting on the ICS proposal, APCIA strongly supports efforts by Team USA to negotiate for IAIS agreement on:

- a plausible way forward for acceptance by the IAIS of an aggregation methodology, and
- an explicit commitment to developing a framework by which all capital assessment methodologies can be evaluated for comparable outcomes.

Achieving these commitments will require highly coordinated and assertive leadership by Team USA, which must speak with a unified voice. Strong Congressional support and oversight of these efforts will be critical to the United States' success at this stage in the IAIS' deliberations. APCIA greatly appreciates the Committee's ongoing and bipartisan oversight to ensure that a strategic and coordinated effort remains a high priority for Team USA.

Timing – the IAIS is seeking to lock-in the ICS at its November 2019 Meeting.

At its Annual Conference in mid-November, the IAIS will vote to approve the current MAV-based ICS for a five-year monitoring period before implementation. During that monitoring period, pursuant to terms of the "Kuala Lumpur Agreement" agreed to by IAIS members in 2017 (KL Agreement), IAIS members will be expected to require the 50 or so IAIGs to annually report group capital on an ICS basis to their group-wide supervisors and members of their supervisory colleges. After the monitoring period and adoption of the final version of the ICS, member jurisdictions, including the United States, will be expected to implement the ICS in their home jurisdictions. However, the FRB and the NAIC have already stated that U.S. insurance regulators will not adopt and implement a MAV-based ICS in the U.S.

The KL Agreement also provides for continued consideration of other variations of the ICS:

- GAAP Plus: utilizes local country accounting rules, with certain defined adjustments;
- Internal Models (IM): uses company-specific capital models; and
- Aggregation: adds together the entity capital requirements and capital resources within group; the KL Agreement provides that this approach will be evaluated by the IAIS on the basis of producing comparable outcomes to the MAV-based ICS.

The global insurance industry, Team USA, and several other country regulators recognize that the ICS is severely flawed and will certainly not be fit for purpose by November 2019, even for those jurisdictions that plan to adopt a MAV-based ICS. The IAIS has accepted the possibility that changes may be necessary during the monitoring period, and that a separate IAIS vote will be held on the revised ICS before it is expected to be implemented. In the meantime, however, IAIGs that will report on an ICS basis strongly believe that those results must be kept confidential, since they would likely not be an accurate reflection of the company's solvency position and would be inherently misleading. Some banks, rating agencies and other third parties have already begun asking IAIGs for their ICS results. APCIA's concern is that competitive pressures on those groups may force disclosure of ICS information. Part of the problem rests with the labelling of the "monitoring period" – even the IAIS now admits that the only thing worthy of "monitoring" is how the ICS and its revisions perform over an extended period.

The November 2019 IAIS meeting will also be a critical watershed moment for whether Team USA can achieve IAIS agreement on a process for determining whether the U.S. aggregation method is sufficiently comparable to the ICS so as to be an outcomes-equivalent means to implement the ICS. The IAIS has not arrived at any criteria for determining comparability and does not plan to do so until some undefined point in time during the 5-year monitoring period. Team USA has indicated that most other IAIS members with whom they are engaged in ICS negotiations hold the view that comparability is simply a matter of comparing the resulting numeric ratios of ICS and aggregation; *in other words, any other method must produce a numerical ratio nearly identical to the ICS or else be considered to fail the comparability test*. This view of outcome comparability essentially assumes that the ICS itself – as a metric - is the perfect benchmark for determining comparability. Instead of demanding strict adherence to an unproven and flawed ICS approach as a measure of comparability, Team USA and the U.S. industry are asking the IAIS to (1) develop an independent way by which all methods are compared (including the MAV-based ICS) to unbiased and objective benchmarks, that (2) uses both quantitative and qualitative methods, that (3) defines "outcome" as the point in time corrective supervisory intervention is triggered by each system, and that (4) makes a comparison on that basis.

What Team USA should seek instead

- Team USA should insist that, before moving forward with adoption of the MAV-based ICS , the IAIS adopt a clear process for creating a comparability framework, based upon independent standards, by which aggregation, the MAV-based ICS, internal models, GAAP Plus, and other jurisdictional group capital assessment methods can be evaluated by the IAIS as achieving comparable outcomes in policyholder protection. The U.S. cannot – and state regulators have indicated that they will not – adopt and implement an ICS that is based upon market-adjusted valuation, as it is inconsistent with the U.S. regulatory system. Put simply, the ICS cannot be considered a global capital standard if the world's largest market – the United States – is not included. There must be clear, unbiased means for both the aggregation method and the MAV-based ICS to be assessed against impartial standards in determining whether the aggregation method may trigger supervisory action *at a similar point* as the ICS.

- Team USA should insist that the IAIS clarify: (1) that the ICS is not fit for **any** purpose during the period 2020-2024, other than to test how it behaves over a period of years, and that the ICS will be subject to significant revisions as necessary with appropriate consultation with stakeholders; (2) that the IAIS will seek consensus that a revised ICS is fit for purpose **before** requesting its adoption and ultimate implementation by member jurisdictions; and (3) that individual company ICS results should be kept strictly confidential during the monitoring period. These commitments are essential to ensure that IAIGs are not harmed during the period by a standard that does not provide an accurate picture of capital adequacy. The IAIS should also consider using a different label than "monitoring period", one that cannot be read to imply that ICS is useful to third parties for any purpose.

- U.S. insurance groups should not be required to report on an ICS basis during that period but can do so voluntarily. Since U.S. regulators have made it clear that the MAV-based ICS will not be required in the U.S. and that an aggregation method will be implemented instead, it would be costly and senseless to require U.S. IAIGs to also provide a MAV-based ICS report. That said, we understand that eight U.S.-based groups are participating in IAIS field testing on a voluntary basis, and nothing should prevent them from continuing with the monitoring period reporting should they so choose.

- Team USA needs to be committed to constructive engagement now and in the long-term and empowered and encouraged to apply the full authority of the United State to insist on a favorable resolution of these issues. Team USA should stand firmly united against moving forward with the ICS 2.0 if there is not an appropriate part to that outcome.

- **U.S. success at the IAIS in November will require a complete commitment and high-level leadership by Team USA, strong support and urging from Congress, and full cooperation from the U.S industry**

APCIA appreciates the efforts of all the members of Team USA to represent U.S. interests at the IAIS and to maintain a unified commitment to an ICS that reflects the U.S. state-based regulatory system, and we have worked hard to encourage continually increased cooperation among them. It is critical now more than ever that Team USA unite behind a strong U.S. position and advocate it vigorously at the IAIS, using all the appropriate resources, political capital, and leadership at this pivotal watershed moment -- not only at the November IAIS committee meetings and Annual General Meeting in Abu Dhabi, but during the preceding meetings of key IAIS working groups and its Executive Committee during September and October. This Committee's hearing comes at exactly the right time to promote and reinforce this unity, political will, and commitment.

Team USA should also be encouraged not to make concessions to other parties within the IAIS without receiving an appropriate quid pro quo in return. It is essential that, at the time when key decisions are made, both the U.S. and European sides have something important at stake. One-sided negotiations have not worked well during this process. In particular, adoption of internal models as part of the ICS must be accompanied by acceptance of the aggregation method as an outcomes-equivalent basis for implementation of the ICS in the U.S.

Conclusion

The IAIS is trying to move forward with proposed global group capital standards that have been criticized as unfit for purpose by the U.S. state insurance regulators, Treasury, the FRB, and much of the global insurance industry. APCIA hopes that Congress will make it a priority to ensure that Team USA remains united and committed to working closely together, domestically and internationally, with the support of the marketplace, to demand a better deal -- one that will work for the U.S. marketplace and recognize and accept the U.S. system. We thank the Committee for underscoring the importance of this effort.