NAMIC®
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

February 13, 2012

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

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429

Office of the Comptroller of the Currency
250 E Street, SW.
Mail Stop 2–3
Washington, DC 20219

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street NE.
Washington, DC 20549–1090

Re: Comments on Volcker Rule Proposed Regulations

Board: Docket No. R–1432 (RIN 7100-AD82)
FDIC: RIN 3064–AD85
OCC: Docket No. OCC-2011-14 (RIN 1557–AD44)
SEC: Release No. 34–65545; File No. S7–41–11

RIN 3235–AL07

Dear Sirs/Madams:

The National Association of Mutual Insurance Companies ("NAMIC") appreciates the opportunity to provide comments regarding the notice of proposed rulemaking[1] (the "Proposal") to implement Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Volcker Rule") to the Board of Governors of the Federal Reserve (the "Board"), the Federal Deposit Insurance Corporation (the "FDIC"), the Office of the Comptroller of the Currency (the "OCC") and the Securities and Exchange Commission (the "SEC") (collectively the "Agencies") .

NAMIC is the largest and most diverse national property/casualty insurance trade and political advocacy association in the United States. Its 1,400 member companies write all lines of property/casualty insurance business and include small, single-state, regional, and national carriers accounting for 50 percent of the automobile/homeowners market and 31 percent of the business insurance market. Since its inception in 1895, NAMIC has been advocating for a strong and vibrant insurance industry.

Background

Section 619(a) of the Dodd-Frank Wall Street Reform Act ("Dodd-Frank")[2] prohibits banking entities from engaging in proprietary trading and from investing in or sponsoring hedge funds and private equity funds. Congress recognized the importance of appropriately accommodating the business of insurance and provided an exemption from the Volcker Rule for an insurance company acting on behalf of its general account. Section 619(d)(1)(F) provides that, notwithstanding the prohibitions of Section 619(a), investing in "securities and other instruments described in subsection (h)(4) by a regulated insurance company directly engaged in the business of insurance for the general account of the company and by any affiliate of such regulated insurance company" is a permitted activity.

Further, Dodd-Frank mandated the Financial Stability Oversight Council ("FSOC") to study and make recommendations on implementing the Volcker Rule to "appropriately accommodate the business of insurance within an insurance company, subject to regulation in accordance with the relevant insurance company investment laws, while protecting the safety and soundness of any banking entity with which such insurance company is affiliated and of the United States financial system."

In comments to the FSOC from November 2010, NAMIC noted that investment limitations imposed upon property/casualty insurers affiliated with an insured depository institution would have the unintended consequence of severely restricting investment options, including ones that involve minimal risk. Allowing insurers to continue in their normal regulated investment activity from their general account, including engaging in proprietary trading and ownership of interest in securities, such as private equity and

[1] Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds, 76 Fed. Reg. 68,846 (Nov. 7, 2011) ("Proposal").
[2] Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111–203, 124 Stat. 1376 (2010). ("Dodd-Frank")

hedge funds, is essential to allow insurers to appropriately engage in effective investment strategies, including matching investment portfolios to anticipated liabilities, and to avoid costly premium increases for policyholders. As the proposed rule observes, it is imperative to implement the Volker Rule in a manner that permits a banking entity "to continue to structure its business and manage its risks in a safe and sound manner." [3] This is equally true for insurance companies affiliated with an insured depository institution.

State insurance investment laws impose strict limits on the types of investments that property/casualty insurance companies may utilize from both a qualitative and quantitative standpoint. The general aim of the state insurance investment laws is to protect the safety and soundness of the insurance institution while also protecting the interests of customers by promoting insurer solvency and financial strength. Congress correctly observed the strength of the state-based regulation and oversight of insurance company investment practices and procedures and admonished the Agencies in implementing the Volcker Rule, to "appropriately accommodate the business of insurance within an insurance company, subject to regulation in accordance with the relevant insurance company investment laws."[4]

Subpart B: Proprietary Trading

Section 13 of the Bank Holding Company Act ("BHC Act")[5] generally prohibits banking entities from engaging in proprietary trading. Specific exemptions from the prohibition of proprietary trading are provided under the Volcker Rule for investment activity conducted through the general and separate accounts of an insurance company. Section _.6(c) of the Proposed Rule (the "General Account Exemption") implements Section 13(d)(1)(F) of the BHC Act to permit the purchase or sale of a covered financial position by a regulated insurance company acting for its general account or an affiliate of an insurance company acting for the insurance company's general account. Section _.6(b)(2)(iii) of the Proposed Rule (the "Separate Account Exemption") confirms that the activities permitted "on behalf of customers" under Section 13(d)(1)(D) of the BHC Act include the purchase or sale of a covered financial position for a separate account of an insurance company.

General Account Exemption

NAMIC supports the General Account Exemption as it is necessary to permit insurance companies to continue to engage in sound, fundamental insurance investment practices. The General Account Exemption generally restates the statutory exemption

[3] Proposed Rules, 76 Red. Reg. 68,849 (Nov. 7, 2011).
[4] Section 619(b)(1)(F)
[5] Bank Holding Company Act § 13(d)(1)(D) (as added by Dodd-Frank § 619).

of Section 619(d)(1)(F) of the Volcker Rule by exempting the purchase or sale of a "covered financial position"[6] by an insurance company or its affiliate if:

(i) the insurance company is directly engaged in the business of insurance and is subject to regulation by a state or foreign insurance regulator;
(ii) the purchase or sale is solely for the insurance company's general account and is in compliance with the laws and regulations of the state or foreign jurisdiction; and
(iii) the particular law or regulation has not been determined by the appropriate Federal banking agencies, after consultation with the Financial Stability Oversight Council and the relevant insurance commissioners, to be insufficient to protect the safety and soundness of the banking entity or the financial stability of the United States.

The Proposed Rule defines "general account" as "all of the assets of the insurance company that are not legally segregated and allocated to separate accounts under applicable State or foreign law."[7] To the extent that the requirement that the assets be "legally segregated and allocated to separate accounts" creates uncertainty whether they should be classified as "general account" or "separate account", it appears the asset would be classified as a general account asset. This presumption is particularly important in the context of insurance company operations.

Separate Account Exemption

NAMIC also supports the Separate Account Exemption, which confirms that Section 13(d)(1)(D) includes transactions conducted by a regulated insurance company for a separate account. Under the Separate Account Exemption, the purchase or sale of a covered financial position by a banking entity that is an insurance company is exempted if:

i. the insurance company is directly engaged in the business of insurance and is subject to regulation by a state or foreign insurance regulator;

ii. the insurance company transacts solely for a separate account;

iii. all profits and losses arising from the transaction are allocated to the separate account and inure to the benefit or detriment of the owners of the insurance policy and not the insurance company; and

iv. the transaction is in compliance with the laws and regulations of the state or foreign jurisdiction.

[6] *See* Proposed Rules, Subpart B, Section __.3(b)(3)(ii) (defining "covered financial position").
[7] *See* Proposed Rules, Subpart B, Section __.3(b)(3)(ii) (defining "covered financial position").

Section 13(d)(1)(D) permits the "purchase, sale, acquisition, or disposition of securities and other instruments on behalf of customers." The Proposed Rule, however, does not define customer and NAMIC urges the Agencies to recognize current and prospective customers.

Separate Account Definition

NAMIC believes that since all insurance company investment activity must be conducted either through the general account or separate account of the company that all investments should qualify for either the General Account Exemption or the Separate Account Exemption. As noted earlier if there is any ambiguity, we believe that the investment should be deemed to be for the general account.

The phrase "and not the insurance company" in §__.6(b)(2)(iii)(C) of the Proposed Rule could have the unintended consequence of making certain types of insurance company investments ineligible for the Separate Account Exemption if the profit and loss were deemed as inuring to the benefit or detriment of the insurance company and if these activities were conducted with respect to legally segregated assets of a separate account they could likewise fail to qualify for the General Account Exemption. As such, investments that are sanctioned under applicable state insurance law could be prohibited under the Volcker Rule. Not only would such an outcome be contrary to congressional intent, but would ironically undermine the state investment laws that are designed to promote the safety and soundness and ensure the solvency of insurance companies.

NAMIC supports the Separate Account Exemption and urges the Agencies to amend it further to avoid any circumstance in which an insurance company investment activity conducted through separate accounts could fail to qualify for either the General Account or Separate Account Exemption. NAMIC also requests that the Agencies amend the definition of "separate account in §__ .2(z) of the Proposed Rules as follows:

"*§__ .2(z)(2) - all profits and losses arising from the purchase or sale of a covered financial position or the acquisition or retention of any ownership interest in a covered fund are allocated to the separate account and inure to the benefit or detriment of the owners of the insurance policies supported by the separate account, and not the insurance company.*"

Subpart C: Covered Funds Activities and Investments

NAMIC urges the Agencies to amend subpart C of the Proposed Rule to extend the General Account and Separate Account Exemptions to investments in covered funds by an insurance company. Section _.10 of the Proposed Rule defines the scope of the prohibition on acquisition or retention of ownership interests in, and certain relationships

with, a covered fund. Section _.10(a) of the Proposed Rule implements Section 13(a)(1)(B) of the BHC Act and prohibits a banking entity from, as principal, directly or indirectly, acquiring or retaining any ownership interest in, or acting as sponsor to, a covered fund, unless otherwise permitted under subpart C of the Proposed Rule. Covered funds include traditional hedge funds and private equity funds, as well as other funds, such as certain foreign funds and commodity pools.

Unlike the subpart B limitations on the proprietary trading restrictions for state-regulated insurance companies trading for general or separate accounts, subpart C fails to recognize the legitimate need for insurance company investment in covered funds. The legislative history of Dodd-Frank shows that Congress clearly intended to exclude insurance company activities from the scope of the Volker Rule prohibitions.[8] When considering the legislation, Congress recognized the breadth and diversity of insurance company investment activities and the strength of the existing state-based insurance investment regulatory and oversight structure. Congress was further concerned that insurers not be subject to further restrictions beyond those already imposed under existing law. Thus, a clear reading of congressional intent and a close examination of the rationale for the proprietary trading exemptions for insurance companies should lead one to conclude that the same exemptions should apply to the covered funds restrictions.

Insurance companies invest in covered funds for the same reasons they invest in other types of assets – to ensure a sound investment strategy that will facilitate policy performance over the long-term, to effectively diversify portfolio holdings, and potentially earn higher returns. The ability to diversify an insurance company's investments is important to creating a balanced portfolio. Covered funds, such as hedge funds and private equity funds, provide a means by which companies can reduce correlation risk as they are less highly correlated with traditional stock and bond investments because of their short-term trading strategies. Investment in covered funds permits insurance companies to properly align both income streams and asset class durations with liabilities.[9] The ability to engage in such investment is critical for insurance companies

[8] As originally proposed, the Volcker Rule would have applied to an insurer with a depository institution affiliate in the same manner as any other entity subject to the Volker Rule. However, Congress recognized that applying the Volcker Rule was unnecessary to effectuate the legislative objective and could unnecessarily harm insurance consumers. As a result, the final legislation included specific direction that the Financial Stability Oversight Council study include recommendations to ensure that the implementation of the Volcker Rule appropriately accommodate the business of insurance (Section 13(b)(1)(F) of the Bank Holding Company Act), as well as a special, specific exemption from applying the Volcker Rule in the case of investments for the general account of an insurance company (Section 13(d)(1)(F) of the Bank Holding Company Act). The FSOC Study acknowledged that the insurance language was included in the Volcker Rule because "[t]he investment activity of insurers is central to the overall insurance business model and could be unduly disrupted if certain provisions of the Volcker Rule applied." FSOC, *Study & Recommendations on Prohibitions on Proprietary Trading & Certain Relationships with Hedge Funds & Private Equity Funds*, at 71 (Jan. 2011)

[9] Section 13(h)(2) of the BHC Act defines the terms ''hedge fund'' and ''private equity fund'' to mean ''any issuer that would be an investment company, as defined in the [Investment Company Act], but for section 3(c)(1) or 3(c)(7) of that Act,'' or such similar funds as the Agencies may by rule determine. Given that the

with long-tail policies in which the liability for coverage may not arise for a significant period of time. Lastly, covered funds provide insurance companies with access to high quality assets with potentially higher rates of return than other traditional assets. Restricting the ability of insurance companies to utilize these investment asset classes would frustrate prudent long-term investment planning and introduce competitive disadvantages for insurance companies affiliated with depository institutions. It would be economically punitive for insurers if their investment trading were restricted so that they could no longer utilize their long-established basic business models. For all the reasons stated above, NAMIC urges the Agencies to amend subpart C to include General Account and Separate Account Exemptions for acquisition or retention of ownership interest in a covered fund by a covered banking entity that is an insurance company.

Separate Subsidiaries

In addition to investing in covered funds, various state insurance laws allow an insurance company to invest in, or organize subsidiaries which may invest in, instruments on behalf of the parent insurance company.[10] Under Section 13(d)(1)(F), affiliates of regulated insurance companies are permitted to purchase, sell, acquire, or dispose of assets for the general account of the regulated insurance company. Because such investment activities are specifically permitted, it would be inconsistent to deem the affiliate a covered fund sponsored by the insurance company, an activity prohibited under § __.10(a) of the Proposed Rule. As such, NAMIC urges the Agencies to permit insurance companies to organize or invest in wholly-owned subsidiaries or affiliates for the purpose of making investments, as permitted under applicable state insurance law, without that subsidiary being deemed a covered fund for purposes of the Proposed Rule. NAMIC further urges the Agencies to specifically exclude insurance company subsidiaries established under state insurance law from the definition of "covered fund." Such exemptions are consistent with the logic of the proprietary trading exemption and the legislative intent of Dodd-Frank that the Agencies accommodate the business of insurance.

Subpart D: Compliance Program

Sections _.7 and _.15 of the Proposed Rule require that a banking entity engaged in proprietary trading or covered fund activity comply with detailed reporting and recordkeeping requirements. Subpart D, § _.20 of the Proposed Rule implements Section 13(e)(1) of the BHC Act, which requires certain banking entities to develop and provide for the continued administration of a program reasonably designed to ensure

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statute defines a ''hedge fund'' and ''private equity fund'' synonymously, the proposed rule implements this statutory definition by combining the terms into the definition of a ''covered fund.'' See proposed rule § _.10(b)(1)

[10] *See* New York Insurance Law Section 1701(a) (permitting a life insurance company to "invest in … subsidiaries engaged" in lawful business activities, including investing); see also Connecticut Insurance Code Section 38-102d(a)(2); New Jersey Insurance Code Section 17B:20-4(d).

and monitor compliance with the prohibitions and restrictions on proprietary trading and covered fund activities.

Section _.20(d) of the Proposed Rule clarifies that, if a banking entity does not engage in covered trading activities and/or covered fund activities or investments, it will have satisfied the requirements of the section if its existing compliance policies and procedures include measures designed to prevent the entity from becoming engaged in such activities or making such investments. An examination of the accounting, investment, and reporting requirements for insurance companies imposed and enforced under state laws demonstrates that the existing regulatory regime is clearly sufficient to ensure insurance company compliance with all applicable restrictions.

States have investment laws that specify which types of assets domestic insurers may hold. Many of those laws also prescribe limits on the amounts of each type of asset that an insurer may hold, as well as limits on the amount of investments in a single issuer that an insurer may hold. Additional state laws typically require the adoption of a written investment plan, including standards for the acquisition and retention of investments by the insurance company and oversight by its Board of Directors. State insurance laws also ensure that investments are valued correctly. The National Association of Insurance Commissioners' ("NAIC") accreditation standards, require that securities be valued according to the rules of the NAIC's Securities Valuation Office[11] and that other invested assets be valued according to the rules of the NAIC's Financial Condition (E) Committee.

Finally, state insurance regulators provide effective enforcement of the stringent financial and investment requirements. The NAIC's Model Law on Examinations, adopted in essence by nearly every state, requires each state's insurance department to conduct an on-site examination of each company domiciled in that state every three (in older versions of the law) or five years. Full- scope examinations are extremely thorough and include review of management and internal controls, corporate records, accounts, financial statements, and asset quality.

Section 13(d)(1)(F) recognizes the validity of state insurance law and regulation unless the Federal banking agencies make a showing otherwise. Based on the breadth and quality of the state reporting and examination process and the statutory recognition of the state regulatory system, it is appropriate to exempt insurers from reporting and recordkeeping requirements of §§ __.7, __.15, and __.20 of the Proposed Rules, including the compliance program requirements of Subpart D. An exemption for insurance companies from these recordkeeping, reporting, and compliance requirements is consistent with the Agencies' view that compliance with adequate existing policies will constitute compliance. Further, appropriate exemptions for insurance company actions under subparts B and C would further exclude insurers from compliance with subpart D.

[11] The SVO is a NAIC staff office that assigns asset quality designations (NAIC-1 for the highest quality, through NAIC-6 for obligations in default) and valuations.

Conclusion

NAMIC believes the most effective way to appropriately accommodate the business of insurance while also protecting the safety and soundness of a banking entity subsidiary of an insurance company is to recognize the protections afforded by state regulatory insurance laws and to ensure that the permitted activity in the Volcker Rule applicable to insurance companies by Section 13(d)(1)(F) is implemented so as to not restrict an insurance company from making investments in compliance with such laws.

Specifically, NAMIC strongly supports the General and Separate Account Exemptions for proprietary trading and urges that any ambiguity in the classification of an account be deemed a general account, and that the definition of separate account be clarified. We further urge that the exemptions for proprietary trading under subpart B be similarly extended to ownership or participation in covered funds under subpart C and insurance company subsidiaries and affiliates be excluded from the definition of covered funds. Lastly, we urge the Agencies to respect the authority of the state regulatory oversight process and exempt insurance companies from recordkeeping, reporting, and compliance requirements under §§ __.7, __.15, and __.20 and subpart D.

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