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Fed Takes First Steps Toward Setting Capital Requirements for Some Insurers

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On June 3, the Federal Reserve Board (the "Fed") released an advance notice of proposed rulemaking (ANPR) and began soliciting comments for the conceptual framework for capital standards that it will use when overseeing the two types of insurers for which it has supervisory authority. Under the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, the Fed was given regulatory authority over insurers that own federally insured banks or thrift institutions and those the Financial Stability Oversight Council (FSOC) designates as systemically important insurers (SIIs). The ANPR closely follows the outline of the Fed's intentions regarding the financial regulation of such insurers. These intentions were first articulated in a May 20 speech at the International Insurance Forum by Daniel Tarullo, a member of the Fed's Board of Governors. The Fed intends to use different capital requirement approaches for the two types of insurers. For insurers that own banks or thrift institutions, the Fed would use a "building blocks approach" to determine required capital. Under this approach, insurers would in most instances be able to use the regulatory capital rules that the relevant regulator already applies to each affiliate. In an insurer's case, the capital requirements would be those of the state insurance regulator or, in a non-U.S. insurer's case, the non-U.S. insurance regulator. Each group's aggregate capital would generally be the sum of the individual capital requirements for each member. To determine required capital standards for insurers designated as SIIs—Prudential Financial, Inc. and American International Group are currently the only insurers designated as SIIs—the Fed would use a "consolidated approach" based on generally accepted accounting principles but modified due to the difference in accounting standards under which insurers operate. For SIIs, the consolidated approach would categorize an entire insurance firm's assets and insurance liabilities into risk segments, apply appropriate risk factors to each segment at the consolidated level, and set a minimum ratio of required capital. The regulatory capital required of SIIs and bank holding companies would appear to be similar. Though, as Tarullo said in his speech "the CA [consolidated approach] would use risk weights or risk factors that are more appropriate for the longer-term nature of most insurance liabilities."

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