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VIA ELECTRONIC TRANSMISSION
www.regulations.gov

February 9, 2012

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

The Honorable John G. Walsh
Acting Comptroller of the currency
Department of the Treasury
250 E St, SW
Mail Stop 2-3
Washington, DC 20219

The Honorable Martin J. Gruenberg
Acting Chairman
Federal Deposit Insurance Corporation
550 17th St., NW
Washington, DC 20429

The Honorable Mary L. Schapiro
Chairman
Securities & Exchange Commission
100 F St., NE
Washington, DC 20549-1090

Re: Notice of Proposed Rulemaking on Restrictions on Proprietary Trading and Certain Interests In, and Relationships With, Hedge Funds and Private Equity Funds (FRS Docket No. R-1432 & RIN 7100 AD 83; OCC Docket ID OCC-2011-14; FDIC RIN 3064-AD 85; SEC File Number S7-41-11).

Dear Sirs and Madam:

Nationwide Mutual Insurance Company and its affiliated companies (collectively, "Nationwide") appreciate this opportunity to comment on the Notice of Proposed Rulemaking ("Proposed Regulations") by the Office of the Comptroller of the Currency ("OCC"), the Board of Governors of the Federal Reserve System ("Board"), the Federal Deposit Insurance Corporation ("FDIC"), and the Securities and Exchange Commission ("SEC") (collectively, the "Agencies") that would implement Section 619 of the Dodd-Frank Wall Street Reform and Consumer

Protection Act ("Dodd-Frank Act") which added a new section 13 to the Bank Holding Company Act of 1956 ("BHC Act"). This new section of the BHC Act sets forth certain prohibitions and restrictions on the general ability of a banking entity and nonbank financial company supervised by the Board to engage in proprietary trading and have certain interests in, or relationships with, a hedge fund or private equity fund. This amendment is commonly known as the "Volcker Rule."

For more than 80 years, Nationwide's insurance and financial products and services have helped millions of Americans protect what matters most to them— their homes, their cars, their businesses, and their financial security as they prepare to live in retirement. The company's mutual standing is a reflection of its roots and historical strength. Mutual ownership enables us to focus more on customers and to make decisions and investments with a longer-term perspective than many of our publicly traded peers that often must focus on short-term results. Moreover, Nationwide is in the business of managing risk. When the 2008 financial crisis erupted, Nationwide was prepared with a strong balance sheet and significant capital on hand. As the severity of the crisis became evident, the company took immediate action to reduce risk, enhance liquidity and preserve capital. Nationwide did not seek or need federal bailout funds from the Troubled Asset Relief Program. Nationwide's preparation and decisive actions ensured that the company remained stable and financially sound.

As a mutual insurance company, Nationwide functions with the interest of its policyholders and members at the forefront in its daily decision-making. It is with this background of a strong mutual heritage and our experience with providing customer-driven products while managing risk through challenging times, that Nationwide respectfully comments on the Agencies' Proposed Regulations. Solely as a result of its ownership of Nationwide Bank, which, as of September, 30, 2011, represents only 2.7% of Nationwide's total consolidated assets, Nationwide is a "banking entity" under new section 13 of the BHC Act and the Proposed Regulations. Nationwide Bank is a federally-insured depository institution regulated by the Office of the Comptroller of the Currency and Nationwide is regulated by the Board as a Savings and Loan Holding Company. Nationwide Bank was formed as part of an overall strategy to more efficiently and effectively serve Nationwide's customers and provide customer-driven products. However, Nationwide Bank represents only a small fraction of Nationwide's business. Yet Nationwide's insurance business, which overwhelmingly represents the company's primary activity, is greatly impacted by its ownership of a relatively small bank. Nationwide's situation in this respect is similar to numerous other insurers.

Congress did not intend for the Volcker Rule to affect the normal business of insurance.[1] While we appreciate the Agencies' efforts to address this Congressional intent, the Proposed Regulations leave insurers such as Nationwide subject to numerous actual and potential restrictions. Congress intended that the Volcker Rule exemption for insurance company general accounts applies both to proprietary trading and covered fund activities.[2] However, the Proposed Regulations do not provide an exemption for covered fund activities. Nationwide requests that the final regulations recognize as a permitted activity investing in covered funds

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[1] *See* 156 Cong. Rec. S5896 (daily ed. July 15, 2010) (statement of Sen. Merkley). This transcript includes the joint statements of Senators Levin and Merkley, the principal authors of the Volcker Rule, explaining Section 13(d)(1)(F), discussed herein as the insurance company general account permitted activity.

[2] *See* bipartisan letter dated January 27, 2012 from 17 members of Congress to the Agencies "emphasiz[ing] that Congress did not intend to prohibit insurance companies from investing in covered funds from their general accounts and we encourage the regulators to make this intent clear in the final rule." *See also* letter dated January 13, 2012 from Senator Kay Hagan urging the Agencies to "conform the rule to Section 619's directive to accommodate the 'business of insurance' and include investments in covered funds with the exception for insurers."

for the general account of regulated insurance companies. For the reasons discussed below, Nationwide also requests that the Agencies exempt insurance company separate accounts from covered fund restrictions. In addition, Nationwide requests that the final regulations reflect appropriate exemptions for insurance companies to organize and offer insurance-related, customer-driven products such as corporate-owned life insurance. Finally, Nationwide requests that the final regulations extend the above-requested exemptions for insurance company general account activity to a subsidiary of the regulated insurance company acting for the general account.

Executive Summary

The Volcker Rule, as implemented by the Proposed Regulations, generally prohibits "banking entities" from engaging in proprietary trading or investing in or sponsoring "covered funds" (a term that includes hedge funds and private equity funds but as currently drafted is so overly broad and ambiguous to capture investment vehicles that have nothing in common with hedge funds or private equity funds). Congress specifically intended to exempt regulated insurance companies from these prohibitions. Congress recognized the unique characteristics and needs of the insurance industry as well as the substantial state insurance regulation over products and investments. Unfortunately, the Proposed Regulations do not reflect this intent and will have a severe and detrimental impact on the insurance industry. Therefore, we urge the Agencies to modify the Proposed Regulations to fully implement Congressional intent with respect to insurance companies.

Specifically, Nationwide requests that the final regulations:

- permit investing in covered funds for the general account of regulated insurance companies;
- exempt insurance company separate accounts from covered fund restrictions;
- permit insurance companies to organize and offer insurance-related, customer-driven separate account products such as corporate-owned life insurance; and
- extend the above-requested exemptions for insurance company general account activity to a subsidiary or affiliate of the regulated insurance company acting on behalf of the insurance company's general account.

The complexity of the Proposed Regulations is evidenced by the many questions the Agencies have posed. With this letter, Nationwide is addressing some of the issues important to the insurance industry. Further, Nationwide is a member of the American Council of Life Insurers (ACLI), the National Association of Mutual Insurance Companies (NAMIC), the Financial Services Roundtable (FSR) and the Committee of Annuity Insurers (CAI). Nationwide fully supports the thoughtful comments by each of these organizations to the Proposed Regulations.

Nationwide Comments

1. Congress Mandated Accommodation of the Business of Insurance

Congress was cognizant of the unique nature of insurance and appropriately recognized that the Volcker Rule, if improperly implemented, could have severe and unintended effects on

insurance companies that have insured depository institutions in their holding company structures. Therefore, Congress initially tasked the newly-formed Financial Stability Oversight Council (FSOC) with conducting a study and recommending implementation so as 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."[3]

The FSOC study recognized that simply applying certain provisions of the Volcker Rule to insurers could be "unduly" disruptive to the business of insurance, stating:

> "Insurance companies assume risk and collect premiums and, in turn, invest those premiums. Investment return contributes to the company's net worth (i.e., policyholder surplus), which in turn supports underwriting and the payment of future claims to policyholders and claimants. The 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."[4]

The Agencies *must* consider the findings of the FSOC study in adopting rules to carry out the Volcker Rule, as directed by Subsection 13(b)(2)(A) of the BHC Act. Congress understood the unique circumstances of insurance companies and, as a result, made special provisions to accommodate them in the Volcker Rule. The final regulations implementing the Volcker Rule must appropriately reflect recognition of this fact.

2. The Law Provides a Permitted Activity Exemption for Regulated Insurance Company to Invest in Covered Funds from its General Account

The plain language of the Volcker Rule provides an exemption from the covered funds prohibition for insurance company general account activity. Subsection 13(a) of the BHC Act sets forth the general prohibition as follows:

> (a) IN GENERAL.— (1) PROHIBITION.—Unless otherwise provided in this section, a banking entity shall not – (A) engage in proprietary trading; or (B) acquire or retain any equity, partnership, or other ownership interest in or sponsor a hedge fund or a private equity fund.

Subsection 13(d)(1) of the BHC Act then sets forth the exemptions from the prohibitions:

> *Notwithstanding the restrictions under subsection (a),* to the extent permitted by any other provision of Federal or State law, and subject to the limitations under paragraph (2) and any restrictions or limitations that the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission, may determine, the following activities (in this section referred to as 'permitted activities') are permitted:

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3 Subsection 13(b)(1)(F) of the BHC Act.

4 See *Study & Recommendations on Prohibitions on Proprietary Trading & Certain Relationships with Hedge Funds & Private Equity Funds*, Financial Stability Oversight Council, January 2011.

* * * * *

> (F) The purchase, sale, acquisition, or disposition of 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, provided that such activities by any affiliate are solely for the general account of the regulated insurance company... (*emphasis added*).

Subsection 13(h)(4) of the BHC Act sets forth the definition of "proprietary trading":

> The term 'proprietary trading'... means engaging as a principal for the trading account of the banking entity or nonbank financial company supervised by the Board in any transaction to purchase or sell, or otherwise acquire or dispose of, *any security*, any derivative, any contract of sale of a commodity for future delivery, any option on any such security, derivative, or contract, or any other security or financial instrument that the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission may ... determine *(emphasis added)*.

The permitted activity in subsection 13(d)(1)(F) is an exemption "[n]otwithstanding the *restrictions* under subsection (a)." This statutory language shows Congress' intent that the permitted activity applies to both the proprietary trading prohibition and the covered fund prohibition set forth in subsection 13(a).[5] We believe that the reference in subparagraph 13(d)(1)(F) to "securities and other instruments *described in* subsection (h)(4)" simply cannot be read to mean that the exemption *only* applies to the prohibition on proprietary trading by insurance company general accounts because (h)(4) does no more than *define* proprietary trading, and subparagraph (F) does no more than *refer* to the instruments described therein.

In other words, Subsection 13(h)(4) is only the definition of "proprietary trading"; it is not the restriction itself. While 13(h)(4) defines the term "proprietary trading", it is referenced only for the purpose of conveniently providing direction to the permissible investments of a regulated insurance company. The reference to this portion of the definition of "proprietary trading" in no way limits the scope of permissible activity only to proprietary trading. The reference to "securities and other instruments described in (h)(4)" in the permitted activity of subsection 13(d)(1)(F) is, therefore, not stating that the permitted activity only applies to the proprietary trading, but rather states that a regulated insurance company may purchase and sell the

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[5] The list of permitted activities would generally apply to both prohibitions -- proprietary trading and investment in or sponsorship of covered funds; however, when Congress intended otherwise, it so stated. Thus Section 13(d)(1)(H) applies only to the proprietary trading restrictions and specifically exempts *"[p]roprietary trading* conducted by a banking entity pursuant to paragraph (9) or (13) of section 4(c), provided that the trading occurs solely outside of the United States..." [emphasis added.] Therefore, this permissible activity by its express scope would not encompass covered funds.

Likewise, Section 13(d)(1)(G) and (I) would apply only to covered funds and lists as permitted activities "[o]rganizing and offering *a private equity or hedge fund*" and "[t]he acquisition or retention of any equity, partnership, or other ownership interest in, or the sponsorship of, a *hedge fund or a private equity fund* by a banking entity pursuant to paragraph (9) or (13) of section 4(c) solely outside of the United States." [emphasis added.] Therefore, the scope of these permissible activities would not include proprietary trading.

securities and other instruments *described in* 13(h)(4) for its general account. The securities and other instruments described in subsection (h)(4) are "*any* security, any derivative, any contract of sale of a commodity for future delivery, any option on any such security, derivative, or contract [emphasis added]." Virtually all investments in private equity funds and hedge funds are securities. Therefore, private equity funds and hedge funds clearly may be acquired by an insurance company for its general account under the permitted activity set forth in 13(d)(1)(F).

The Proposed Regulations recognize the exemption for insurance company general account investment activity from the prohibition on proprietary trading under §__.6(c); however, the Proposed Regulations do not recognize the exemption for insurance company general account investment activity from the prohibition or restrictions on covered fund activity under §__.10(a). Since the Proposed Regulations do not provide an exemption from the covered fund prohibition, an insurance company would be prohibited from investing in covered funds. This position neither reflects the plain language of the statute nor complies with the Congressional mandate to accommodate the business of insurance.

As outlined above, the Volcker Rule expressly exempts insurance company general account activity from both the proprietary trading as well as the covered fund prohibitions. The Proposed Regulations, however, do not recognize the latter exemption from the covered funds prohibition. As a result, this would prohibit an insurer such as Nationwide from investing in covered funds--hedge funds and private equity funds--despite the statutory exemption permitting insurers to do so.

Moreover, if the statute were not read to provide a parallel exemption for covered fund activities by insurance general accounts, it would create an arguably irrational result by permitting an insurance company to obtain exposure to an asset class through its proprietary trading exemption while at the same time prohibiting it from obtaining exposure to the same asset class through the covered fund prohibition.

In addition to the statutory language, there are many sound policy reasons why insurance companies should be able to invest their general account assets in covered funds.

First, without recognition of the exception for insurance company general account investment in covered funds, the Proposed Regulations will prohibit insurance companies from pursuing diversified portfolio investments that have a collateral impact on the economy as a whole. These investments generally support economic growth and business development. Insurance company investments into covered funds provide important liquidity to the financial markets and contribute to the economy by providing much needed capital to entrepreneurs and businesses, thereby encouraging job and wealth formation.

Second, because covered funds generally have a longer investment horizon than other investments as well as greater potential returns, they provide diversification for insurer portfolios in a manner that balances investment risk management. Covered funds also provide insurers the ability to invest prudently and soundly in specialized strategies that may not otherwise be available. Depending on an insurer's liability structure, these asset classes may form an integral part of an insurer's overall asset-liability management strategy. Insurers rely on investment income to offset unexpected losses related to weather events. Investment income provides a stabilizing effect on insurance rates that would be lost if the investment opportunities were drastically restricted. Thus, the effect of the Rule would adversely impact the ability of an insurer to prudently manage its investment portfolio in light of the asset and liability structure and mix of an insurance company for which covered funds are a critical component. Moreover,

since the Volcker provisions do not apply to all insurers, such restrictions would create an unlevel playing field within the insurance industry.

Finally, the prohibition does not serve any compelling public purpose. The Volcker Rule was enacted to protect the safety and soundness of banking entities and the financial system. Insurers are already subject to substantial regulation at the state level for this same purpose. In fact, the Proposed Regulations could have the opposite effect on insurer solvency. If finalized as proposed, the Proposed Regulations could immediately force insurance companies to sell heavily regulated and permissible investments, likely at steep discounts. This will almost certainly have a negative impact on the financial flexibility of affected insurance companies, placing them at greater financial risk both in the short term, due to the "forced" sale of securities into the very illiquid secondary market for privately negotiated instruments, as well as the long term, due to the inability to invest in an important asset class effectively used for diversification and asset allocation purposes. And as noted above, the Volcker Rule going forward would hamper sound risk and investment management of an insurer's investment portfolio to meet policy obligations.

Congress must not have viewed the traditional business of insurance as a threat to the safety and soundness of the United States financial system. If it had, it easily could have subjected *all* insurance companies to the Volcker Rule. To the contrary, Congress expressly exempted insurance companies doing business for their general account from both the proprietary trading and covered funds prohibitions of the Volcker Rule. The Agencies implementing the Volcker Rule should do likewise. Accordingly, Nationwide requests that the Agencies specifically recognize the permitted activity of an insurance company to purchase, sell, acquire and dispose of covered funds in its general account.

3. Final Regulations Should Specifically Recognize the Traditional Business Model of Insurance

The foundation of the traditional business model of insurance is built on the underwriting and management of large diversified pools of risks. Insurance companies manage these risks through asset-liability management. That means that the insurer must determine what its expected claims will be and when it will need to pay money out to its customers under its insurance policies. The insurer then must manage the maturity and return on its assets to fund these expected liabilities. This ensures that the company can meet its promises to its customers when they arise. Appropriate asset-liability management is integral to the insurance business model and is vital to the survival of an insurance company.

In considering asset-liability management by insurance companies, particular consideration must be given to the investment function. Insurance investments must cover the provisions for expected claims and policyholder benefits. In many cases, these insurance-related liabilities are longer-term in nature and thus help to insulate insurers from short-term shocks to the financial system. The longer time horizons, however, do not imply that insurers pursue mere buy-and-hold investment strategies. Rather, most insurers actively manage their investment portfolios with a careful eye to maximizing their risk-adjusted returns consistent with their liability structures.

As discussed above, the funding model for insurance companies, for example, is fundamentally different from that of traditional banks and other financial firms. Unlike banks, insurance companies do not rely on short-term borrowings to fund their operations. Instead, the longer-term liability structure of insurance companies means that they need, as a business and

regulatory matter, to rely on longer-term assets to support their liabilities. The Volcker Rule expressly incorporates Congressional understanding of the differences between the insurance company business model and the business model of other financial institutions; final regulations must do so as well.

4. State Insurance Laws and Regulations Protect Against Risky Investment Practices

Congressional recognition of the special characteristics of insurance companies was based in no small part on the extensive and robust state investment law regime to which insurance companies are already subject. For example, state insurance company investment laws generally include (but are not limited to) specific limits on asset types such as investments in equities, mortgages and lower-grade securities. They also generally limit the amount of investments in any one issuer or property. This encourages diversification of insurer investments by both asset class and by issuer. Insurance laws only allow insurers to include assets that meet these requirements as "admitted" assets on their balance sheets for purposes of determining whether the insurer can discharge its obligations and meet state capital and surplus requirements.

Congress set a high bar for overriding a state insurance law. Subsection (d)(1)(F)(ii) of Section 13 of the BHC Act provides that the only way that state insurance laws may be overridden is in the situation where the Agencies, along with the FSOC and the relevant state insurance commissioners, have determined that a state insurance investment law is insufficient to protect the safety and soundness of the insurer.[6] It is important to note that the Proposed Regulations specifically state that the Agencies have not made any such determination.[7]

The extensive state regulatory system to which insurance companies are already subject is designed to ensure the safety and soundness of the insurance company so that customers' promises will be fulfilled. These investment laws have been specifically designed by state authorities with long-standing and in-depth insurance expertise. As previously noted, these investment laws provide exposure limits to particular types of asset classes as a percentage of admitted assets, allowing insurance companies to properly diversify risk among investment classifications, thereby enabling them to support their long-term liabilities with appropriate long-term assets.

In addition to statutory investment limitations by asset type and issuer, insurance company investment activities are subject to comprehensive inspection regulation and oversight under state law. For example, state insurance regulators have broad oversight and examination power of all insurance company investments to ensure that the investments are in compliance with state insurance investment regulations and that the investments do not threaten the solvency of the insurance company. As part of this regulatory regime, insurance companies are required to file annual financial reports covering their investment and other activities, and are required to meet and report certain risk-based capital ratios. By addressing various parts of the

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[6] Subsection (d)(1)(F)(ii) of Section 13 of the BHC Act provides that:

> "[t]he appropriate Federal banking agencies, after consultation with the [FSOC] and the relevant insurance commissioners of the States..., have not jointly determined, after notice and comment, that a particular law, regulation, or written guidance described [above] is insufficient to protect the safety and soundness of the banking entity or of the financial stability of the United States."

[7] See footnote 172, p.76.

insurance company's risk profile, including its statutory reserves, capital adequacy and overall solvency, the state insurance law regime serves as an effective mechanism for regulating insurance company investment activities.

The Volcker Rule as codified in new Section 13 of the BHC Act recognizes the importance of state insurance laws. Most state insurance investment laws allow for insurance company investments into covered funds subject to certain strict requirements, such as a limitation as a percentage of admitted assets. State regulators recognize the importance of such investments for diversification and portfolio management strategies, while at the same time placing prudent, conservative limitations on the extent to which an insurance company can avail itself to this class of investments.

5. The Agencies Should Recognize the Permitted Activity Exception for Insurance Company Separate Account Investment in Covered Funds and Other Conventional Separate Account Activity

Separate accounts are created and regulated under state insurance laws and/or federal securities laws. Widespread, varied usage of separate accounts is an integral component of modern life insurance companies. The use of separate accounts in accordance with state insurance law guidelines and regulatory oversight allows insurance companies to develop customer-driven insurance products tailored to meet the specific demands of an increasingly diverse market.

Insurance companies use separate accounts to provide insurance-related products for fully-informed consumers who choose to assume the risk associated with investments tied to those products. At the core of most such arrangements is customer assumption of investment risk. Therefore, far from subjecting life insurance companies to financial risk, these arrangements most frequently shield the life insurance company from investment risk—as such, these activities, even if they include investment in covered funds, should be exempted from Volcker Rule prohibitions.

In order to clarify the impact of the Proposed Regulations on insurance company separate accounts, and to adhere to the Congressional mandate to accommodate the business of insurance, Nationwide recommends that the Proposed Regulations recognize certain permitted activities related to insurance company separate accounts.

a. Separate Account Investment in Covered Funds Should be Considered "On Behalf of Customers"

In addition to incorporating the statutory insurance company general account exemption discussed above, the Proposed Regulations also recognize the statutory exemption for certain insurance company separate account investment activity from the prohibition on proprietary trading under §__.6(c). However, as in the general account context, the Proposed Regulations do not extend this exemption to covered fund activity under §__.10(a). Again, this position neither reflects the plain language of the statute nor does it reflect the Congressional intent to accommodate the business of insurance.

As with insurance company general account activity, the plain language of the Volcker Rule mandates an exemption from the covered funds prohibition for insurance company separate account activity. Subsection 13(d)(1)(D) of the BHC Act sets forth the exemptions from the prohibition for activity "on behalf of customers" by permitting:

> (D) The purchase, sale, acquisition, or disposition of securities and other instruments *described in* subsection (h)(4) on behalf of customers *(emphasis added).*

The permitted activities in subparagraphs (D) and (F) provide the exact same reference to "securities and other instruments *described in* subsection (h)(4)." Therefore, as discussed previously, the applicability of each permitted activity is not referencing exclusively the restriction against proprietary trading, but rather only the securities and other instruments *described in* (h)(4). The securities and other instruments described in subsection (h)(4) are "any security, any derivative, any contract of sale of a commodity for future delivery, any option on any such security, derivative, or contract, or any other security or financial instrument that the appropriate Federal banking agencies, the Securities and Exchange Commission, and the Commodity Futures Trading Commission may ... determine." Virtually all private equity funds and hedge funds are within the legal definition of "securities" that may be acquired under 13(d)(1)(D); therefore, the plain language clearly indicates that the "on behalf of customers" exception set forth 13(d)(1)(D) applies to the covered fund prohibition as well as the proprietary trading prohibition,(see Comment 2 above).

Just as with general accounts, the Agencies should not unduly restrict the insurance industry's use of separate accounts in developing products that meet discrete market and customer needs and preferences. A salient aspect of products associated with separate accounts that permit investment in covered funds is the assumption of inherent investment risk by consumers. Consequently, investments in covered funds through a traditional separate account do not expose the insurance company to investment gains or losses in that separate account.

The Volcker Rule as codified in subsection 13 (d)(1)(D) of the BHC Act expressly exempts activity conducted "on behalf of customers" from both the proprietary trading as well as the covered fund prohibitions. The Agencies have recognized that activity by an insurance company in a separate account is "on behalf of customers" of the insurance company and, on this basis, have included in the Proposed Regulations an exemption for insurance company separate account activity from the prohibition on proprietary trading. However, the Proposed Regulations do not provide an exemption for investment in covered funds by separate accounts. This would prohibit an insurer such as Nationwide from investing in covered funds even for separate accounts associated with products that pass investment risk to consumers. This position, again, fails to reflect the Congressional mandate to accommodate the business of insurance. Nationwide requests that the Agencies specifically recognize the permitted activity of an insurance company to purchase, sell, acquire and dispose of covered funds in a separate account.

b. Separate Account Accrued Charges and Seed Money Should be considered "Profit and Loss"

The Proposed Regulations provide that an insurance company is permitted to engage in proprietary trading for a separate account under §__.6(b)(2)(iii) so long as certain conditions are met, including the following:

> (C) All profits and losses arising from the purchase or sale of a covered financial position 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* (*emphasis added*).

However, existing insurance laws allow an insurance company to allocate or transfer its own funds to certain separate accounts with the profits or losses on those funds inuring to the benefit or detriment of the insurance company. This initial allocation to certain separate accounts is referred to as "seed money" and must often be contributed by the insurance company to facilitate initial operations. In addition, a separate account may periodically include accrued insurance charges such as mortality, expense and cost of insurance charges. The use of seed money within separate accounts and the existence of accrued charges may not represent assets associated with the profit and loss experience of customers but are nevertheless merely incidental for purposes of facilitating separate account arrangements.

In light of this practical, substantive assessment of the manner in which separate accounts are actually constructed and operated, we believe an accommodation for the use of seed money and the existence of accrued charges within separate accounts operated "on behalf of" customers is quite obviously consistent with the overall purpose of the statute and the Proposed Regulations. Nationwide requests that the Agencies recognize the permitted use of "seed money" and existence of accrued charges in separate accounts in the final regulations.

c. Separate Accounts Are Not Covered Funds And Are Not "Sponsored" by Insurance Companies

Many commenters have pointed out to the Agencies the numerous and significant unintended consequences that will flow from the overly broad proposed definition of "covered funds," which goes far beyond those structures Congress intended to capture--hedge funds and private equity funds. As the Proposed Regulations are drafted, "covered funds" would capture many insurance company separate accounts. These separate accounts have little in common with hedge funds and private equity funds and undoubtedly were not the type of structure that Congress was considering. We urge the Agencies to use their rulemaking authorization to narrow the definition of covered funds so that it appropriately applies to hedge funds, private equity funds, and similar funds and does not sweep up the panoply of investment vehicles that, while they look nothing like hedge funds or private equity funds, nonetheless rely on Section 3(c)(1) or 3(c)(7) of the Investment Company Act of 1940 (the "1940 Act").

Separate accounts are created and regulated under state insurance laws and may, depending on the manner in which they are used, be exempted from registration and other substantive provisions of the 1940 Ac t. The exemptive provisions under Section 3(c)(1) or 3(c)(7) of the 1940 Act may be invoked for these purposes. Although separate accounts and private equity funds or hedge funds may share the path to exemption from the 1940 Act through reliance on Section 3(c)(1) or Section 3(c)(7), they are in fact completely different arrangements; these separate accounts should not be considered synonymous with private equity funds and hedge funds for purposes of the prohibition on sponsorship of Covered Funds. In connection with such offering of insurance-related products, an insurance company may also be deemed to "sponsor" such unregistered separate accounts within the technical language of the Proposed Regulations. The definitional elements of the term "sponsor" presuppose that the fund is a separate legal entity from the sponsor and that the sponsor maintains one of the three statutorily specified relationships with the separate legal entity.

An insurance company does not "sponsor" a separate account within the meaning of this term as used in the Volcker Rule. A separate account simply represents a segregated pool of assets on the balance sheet of an insurance company that supports a specific policy claim on the insurance company. It is not a separate legal entity from the insurance company itself. Thus, a separate account does not constitute a separate legal entity as envisioned by the Volcker Rule. In any event, an insurance company does not possess any of the elements of the definition of "sponsor" because it does not "serve as a general partner, managing member or trustee" of an unregistered separate account, nor does it "select or control . . . a majority of the directors, trustees or management" of an unregistered separate account or "share" a name with a separate account. The use of the term "sponsor" in this context would lead to the hopefully unintended result that separate accounts--which are integral to the traditional business of insurance companies--would be prohibited. Nationwide requests that the Agencies specifically recognize that an insurance company organizing a separate account is not "sponsoring" a covered fund as contemplated under the Volcker Rule.

d. Separate Accounts for Corporate-Owned Life Insurance Products Should Have the Same Treatment as Bank-Owned Life Insurance (BOLI) Products

The Proposed Regulations specifically permit acquiring and retaining an ownership interest in, or acting as sponsor to, certain BOLI separate accounts. This exemption permits: (1) insurance companies to sponsor a separate account for BOLI products, and (2) banking entities to purchase and own insurance policies invested in or supported by a 3(c)(1) or 3(c)(7) separate account. Nationwide supports this provision.

The plain language of the Proposed Regulations prohibits other products of this same structure, such as corporate-owned life insurance (COLI), in which the only significant difference from BOLI is that the customer is not a bank. The rationale for the BOLI exemption is that the investment risk is borne by the policy owner. This is consistent with the definition of separate account under state law in that the income, gains and loses on assets in the account are credited to or charged against the separate account. In addition, this separate account activity by insurers is subject to regulation and supervision by the state insurance regulators. These rationales apply equally to section 3(c)(1) and 3(c)(7) separate accounts used in contexts other than BOLI, such as COLI and certain high net-worth private placement products. These types of separate account products offer the customer the needed protection and return profile they require. Nationwide requests that the Agencies recognize an exception for separate accounts products like COLI, similar to the BOLI product exception.

6. Permitted Activities and Exceptions Should Apply to Insurance Company Investment Subsidiaries

State law permits an insurance company to organize subsidiaries for the purpose of investing according to state law. Often, these subsidiaries (or affiliates) rely on section 3(c)(1) or 3(c)(7). The Proposed Regulations would prohibit an insurance company from organizing such a subsidiary because it would technically fall within the definition of a covered fund. Nationwide requests that the permitted activities and exceptions discussed herein apply equally to a subsidiary that is not a federally-insured depository institution.

7. Economic Impact of Volcker Rule

Congress clearly intended that the Agencies appropriately accommodate the business of insurance when implementing the Volcker Rule, as evidenced by its call for the FSOC study and its inclusion of insurance-related exemptions in the statute. However, if adopted, the Proposed Regulations could have a sharply negative impact on the insurance industry specifically and on the broader markets generally. Insurance companies with a federally-insured depository institution in their holding company structure, regardless of its relative size, would essentially be hamstrung from conducting the business of insurance.

Private equity fund and hedge fund investments generally require long term commitments of capital. Absent extensions, the Proposed Regulations would require firms to comply with the prohibitions of the Volcker Rule by July 21, 2014. The requirement to comply in this time frame would necessitate the "forced" sale of billions of dollars of investments in the secondary market. Given the fact that the insurance industry represents one of the largest investors in private equity and hedge funds, this would likely result in steep discounts to their fair value, leading to major economic losses to the insurance industry. This scenario and a prohibition going forward would place individual insurance companies that own small banks at a financial disadvantage, could compromise sound and effective risk and management of an insurance company portfolio and could conceivably adversely impact the entire U.S. financial system. Most importantly, these losses would inevitably result in higher costs or lower benefits to the ultimate consumers who rely on insurance products to protect their assets. Even assuming the conformance period is extended beyond 2014, the unfunded liabilities involved in these investments in many cases extend beyond any possible conformance period.

The uncertainly of the Proposed Regulations is already having a negative impact to Nationwide and other insurers. Specifically, this uncertainty has forced Nationwide to reevaluate its investment policies to protect its customers from a potentially negative outcome as a result of the implementation of the Volcker Rule.

Conclusion

Congress intended to exclude insurance companies from the Volcker Rule prohibitions and, therefore, tasked the Agencies with implementing the Volcker Rule in a manner designed to appropriately accommodate the business of insurance. Accordingly, the Proposed Regulations should clearly exclude from the prohibitions companies engaged in the business of insurance and provide for appropriate exclusions for insurance-related products. Investment activities relating to proprietary trading, private equity and hedge funds and general and separate accounts are all central to the business of insurance and they pose no undue risk to the safety or soundness of the insurance company or the financial system. To the contrary, a wide variety of investments permissible and regulated under state law supports the diversification appropriate to an insurer's asset-liability mix and, therefore, the financial soundness and solvency of insurers. In addition, the Proposed Regulations should not have the unintended effect of eliminating an insurer's ability to offer certain insurance products. Therefore, Nationwide requests that the Proposed Regulations clearly exclude insurance company general account and separate account activity as set forth herein from the Volcker Rule prohibitions.

As always, we appreciate the dialogue and look forward to further opportunities to comment.

Very truly yours,

NATIONWIDE

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