September 25, 2012

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. 2012-200 - Proposed Accounting Standards Update, Financial Instruments (Topic 825) - Disclosures about Liquidity Risk and Interest Rate Risk

Dear Technical Director:

Nationwide Insurance appreciates the opportunity to comment on the Exposure Draft of the Proposed Accounting Standards Update, Financial Instruments (Topic 825) - Disclosures about Liquidity Risk and Interest Rate Risk (ED or proposed ASU). The Nationwide Insurance Enterprise (Nationwide) is comprised of three affiliated mutual insurance companies and their subsidiaries under common management, operating both property and casualty (P&C) and life insurance companies. Nationwide is one of the largest diversified insurance and financial services organizations in the world with U.S. GAAP annual revenues of $19 billion and assets totaling $155 billion.

We support the Board’s efforts to address constituents’ concerns that the existing disclosures do not provide adequate information about liquidity and interest rate risks that arise from an entity’s financial instruments. We also agree with the Board’s stated objective to provide users with greater consistency and comparability. However, we do not believe the standardized approach proposed by the Board would achieve this objective. Instead the proposed ASU, as it is currently written, would provide users with complex and misleading information about an insurer’s exposure to liquidity and interest rate risk, because the proposed disclosures do not accurately reflect an insurer’s business model and risk management strategies. Furthermore, the considerable increase in the amount of disclosures would result in significant resource demands and costs to develop processes needed to comply with the new disclosure requirements. We believe the costs associated with implementing the proposed disclosures outweigh the benefits.

Within this comment letter, we will expand on our concerns and share our views on certain clarifications and simplifications that should be made to minimize implementation complexities and ensure that the information is understandable to financial statement users. Below is a list of our primary concerns:

- These disclosures would be more useful if they contained forward-looking information, and placed in the Management’s Discussion and Analysis (MD&A) disclosures.
- The definition of a financial institution inappropriately includes P&C insurance entities.
- The liquidity gap table does not fairly represent an insurance company’s management strategy or its liquidity position.
- The interest rate tables do not accurately reflect an insurer’s management strategy or its exposure to fluctuations in market interest rates that arise from its insurance contracts.
- The ED should not require a nonpublic entity that is not a financial institution to identify and present reportable segments solely for the purpose of these proposed disclosures.
- The operational costs to implement the proposed disclosures outweigh the benefits.

Please see below for details on our recommendations.
COMPREHENSIVE RECOMMENDATIONS

The Information within the Proposed Disclosures is more useful in the MD&A
We support the Board’s effort to address stakeholders’ request for more useful and comparative liquidity and interest rate risk disclosures. However, we do not believe the standardized tables along with the qualitative narratives accomplish this objective, particularly for an insurance entity. The proposed disclosures would not: (1) provide relevant information regarding liquidity and interest rate risks related to insurance contracts; (2) reflect how an insurer would manage these risks; or (3) reflect an insurer’s asset-liability management. In order to strike the right balance between comparability and providing relevant information, the proposed tables would require forward-looking assumptions and/or modifications. Our rational supporting why this is necessary is elaborated in the subsections dedicated to the individual disclosures below. We encourage the Board and the SEC to work jointly to determine disclosures that would be more comparable, but without sacrificing the usefulness of the information in understanding an insurance entity’s true exposure to liquidity and interest risks and the different ways it manages those risks. This can be achieved by enhancing the liquidity and interest rate risk disclosures currently required in the MD&A.

The Definition of a Financial Institution should Exclude P&C Companies
We do not believe P&C companies should be considered financial institutions. P&C companies are not spread focused businesses, as such, asset-liability management is not as integral to measure liquidity risk as it is to a spread focused life insurance company. P&C companies generally use cash flows from operations to pay obligations as they come due. This business model is similar to the Board’s description of a nonfinancial institution in the Basis of Conclusion (BC) paragraph 8, which states:

The Board noted that asset-liability management is an integral aspect of liquidity risk for financial institutions; conversely, entities that are not financial institutions generally do not match the maturities of their assets and liabilities and often use cash flows from operations (rather than from existing financial assets) to pay obligations as they come due.

Based on the business model and the liquidity management of P&C companies, we believe the nonfinancial institution disclosures are more appropriate for these companies. This view is further supported by the lack of useful information P&C companies would provide in the proposed tabular interest rate risk tables (see below for additional commentary). Therefore, we recommend the definition of a financial institution explicitly exclude P&C companies.

The Use of Expected Maturities for Insurance Contracts to Highlight Liquidity Risk
The liquidity gap table would require financial institutions to disclose the carrying amounts of classes of financial assets and liabilities, segregated by their expected maturities. This requirement does not fairly represent a life insurance entity’s management strategy or liquidity position as the disclosure requires contractual maturities to be used. Many life insurance products do not have explicit contractual maturities (e.g., variable and fixed deferred annuity products, universal life-type products, whole life insurance products, etc.) and for those that do (e.g., individual term life) policyholders may have the right to continue the policy past the original term. Therefore, expected liability payments would generally appear to be long and, thus bucketed in the ‘5-years from report date’ and ‘thereafter’ columns. Instead of having a contractual maturity date, life insurance products require actuarial estimates of expected death benefit claims, lapses, surrenders, and other actuarial assumptions affecting the amount and timing of expected cash flows for these policies. It would be more meaningful to have the liquidity gap maturity table reflect these actuarial estimates. This information could be analogized to the prepayment expectations that a bank would use in showing the expected maturity of loans to consumers. The ED
should be revised to allow insurers to use their actuarial estimates in the disclosures rather than contractual maturities.

Even if the liquidity gap table were to reflect the actuarial assumptions for the liabilities, the related assets would generally appear in earlier time periods, because a typical life insurer would have a reinvestment strategy, involving investing in shorter-term securities, to settle these long-duration liabilities. Consequently, the life insurer would appear to have a significant asset-liability mismatch, which would be misleading if not accompanied by forward-looking management discussion.

We understand the objective of the proposed liquidity gap table is to provide users with information about the risk that a reporting entity will encounter difficulty meeting its financial obligations. However, we do not believe the proposed disclosure would achieve this objective. In order to do so, we recommend that the Board work with the SEC to incorporate incremental liquidity information into the liquidity risk disclosures currently required in the MD&A. This would require a life insurance entity to discuss its unique liquidity risk management strategies and assumptions, which we believe would be more meaningful to financial statement users.

**Interest Rate Risk Disclosures for P&C Companies**

Interest rate tables, as currently proposed, would not provide useful information about insurer’s exposure to interest rate risk that arises from its insurance contracts. For example, a P&C company would provide little liability information in the interest rate risk tables, because its loss reserves¹ (its only significant policyholder liability) are typically undiscouted unless fixed and reasonably determinable. Therefore, the vast majority of its policyholder liabilities is not directly impacted by interest rates and would therefore not appear in the table. Consider the proposed repricing gap table, which is intended to help financial statement users understand how well a financial institution is matching the duration of its financial assets and liabilities. Since interest rates do not have a direct affect on loss reserves, a P&C company’s repricing gap table would only reflect the weighted-average contractual yield in each time interval, the total weighted-average contractual yield, and duration for its financial assets. The loss reserves would be reflected in the non-interest bearing financial liabilities section of the table, because weighted-average yield and duration would not be applicable. As such, the repricing gap table does not provide meaningful information about how a P&C company manages interest rate risk. The after-tax net income and shareholders’ equity impact derived from the predefined movement in market interest rates would, for the most part, only represent the effect of fair value changes on a P&C company’s financial assets. As noted earlier, we believe it is inappropriate to consider a P&C entity a financial institution, and the lack of useful information it would provide in the proposed interest rate risk disclosures further supports our view.

**Repricing Gap Table – Life Insurance Companies**

The usefulness of the proposed interest rate tables would also be limited for a life insurance entity. The repricing gap table would not properly reflect the interest crediting features found in many life insurance products. Generally, a life insurer is allowed to (but not required to) change the interest rate on a policyholder contract from time to time, subject to minimum floors. Typically, a life insurer would hold crediting rates steady if it is able to maintain its yield from related investments, but it could decrease crediting rates if investment yields decline. For example, in year one a life insurer has a block of $500,000 fixed deferred annuity contracts in which the interest credited rate resets annually and is currently at 4%. In order to match its expected liability payments, management invested in bonds that have a shorter duration than the liabilities.

¹ The loss reserve is the estimated ultimate cost of settling P&C claims relating to insured events that have occurred on or before the balance sheet date. The estimated liability includes the amount of money that will be required for future payments on both: (a) claims reported, and (b) claims relating to insured events that have occurred but have not been reported.
If interest rates were to decrease to 2%, an insurer would appear to have a significant reinvestment risk and an asset-liability mismatch, because the repricing gap table does not take into account the ability to adjust the liability crediting rates.

The repricing gap table implies that all financial institutions are exposed to market interest rate movements. However, for life insurance entities, the true risks are crediting rate floors and the market environment associated with life products. Specifically, the risks are encountered when yields from invested assets are lower than credit rate floors or when an insurer would like to decrease its crediting rates, but does not due to competition from its peers. This spread compression would not be reflected in the repricing gap table. Therefore, we recommend the Board work with the SEC to incorporate repricing information into the MD&A because it requires forward-looking assumptions.

**Interest Rate Sensitivity Analysis – Life Insurance Companies**
The interest rate sensitivity analysis table as currently proposed would mislead many financial statement users because of its prohibition to use forward-looking assumptions. Without the ability to incorporate forward-looking information about policyholder behavior and management’s actions the table would not be relevant. To illustrate this point, consider a life insurer’s life insurance policies not carried at fair value. If management does not reflect changes in crediting rates or policyholder behavior, the instantaneous “shock” scenarios would have no impact on policyholder reserves because there is no component of the calculation of the reserves carrying value that would change.

Based on the above, we believe the standardized interest rate sensitivity table, even when accompanied with qualitative narratives would be misleading without forward-looking management assumptions. In order to provide relevant information to users, we recommend incorporating management’s forward-looking assumptions that the Board work with the SEC to include this disclosure in the MD&A.

**Clarification for Nonfinancial Companies**
The proposal requires a nonfinancial entity to determine whether it has reportable segments that meet the definition of a financial institution. However, the proposed guidance does not specify how a nonpublic entity (which is not required to present reportable segments) would apply this guidance. We encourage the Board to provide a nonpublic entity that is not a financial institution the option to present the required disclosures either at the reportable segment level or operating segment level, or at a minimum provide a nonpublic entity the option to prepare the proposed disclosures based on whether the majority of its business activity is financial or nonfinancial. We do not believe that the benefits from requiring a nonpublic entity to identify and present its reportable segments, strictly for these new disclosures, would outweigh the costs of doing so.

**Operational Costs**
We have many operational concerns regarding the proposed disclosures. Specifically, a significant amount of the data, assumptions, and possible strategic responses are outside of our financial statement reporting process and is therefore not currently subject to audit requirements. The time and expense associated with implementing a new process to make subjective assumptions auditable for the first time would be significant considering the resources and implementation challenges (e.g., developing and adjusting systems and reporting processes, documenting and testing these processes, and implementing and testing internal controls over these new financial reporting processes). We believe it would take many public insurance companies at least 18 months to implement new disclosures and additional time would be needed for nonpublic companies. Unlike public companies, which have provided similar information about their liquidity and interest rate risk exposure in the MD&A sections of their annual reports, these proposed disclosures would be new for nonpublic companies, and therefore would require additional time and effort to implement. As such, we recommend providing nonpublic companies with at least a one year delayed effective date.
CONCLUSION

As noted throughout our letter, insurers would face significant challenges in developing processes to gather, summarize, classify, and report the information necessary to comply with the proposed ASU and make the disclosures relevant to an insurance company. As currently drafted, we believe the associated costs to implement the proposed disclosures outweigh the benefits. We believe that the standardized quantitative disclosures, which do not align with insurers’ business models or risk management strategies, limit the usefulness and understanding of these proposed financial statement disclosures.

In place of the proposed liquidity and interest rate risk disclosures, we recommend that the Board should partner with the SEC to enhance liquidity and interest rate risk disclosures currently required in the MD&A to address stakeholders’ request for comparability and more decision-useful information.

Nationwide’s response to the comprehensive list of questions is attached as an appendix to this letter.

We hope these comments assist you during your re-deliberations of the proposed guidance. In the event that any Board or FASB staff member would like further clarification of our positions, we would be happy to discuss them in greater detail.

Respectfully,

James D. Benson
Senior Vice President, Enterprise Controller and Chief Accounting Officer
Nationwide Insurance
APPENDIX

QUESTIONS FOR RESPONDENTS

Questions for Preparers and Auditors—Liquidity Risk

Question 1: For a financial institution, the proposed amendments would require a liquidity gap table that includes the expected maturities of an entity’s financial assets and financial liabilities. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

Yes, we do have operational concerns. An insurer would have to modify systems, reporting processes, and document and test internal controls over these new financial reporting processes to ensure its external auditors could obtain reasonable assurance over the proposed disclosure. We believe the costs of implementing the liquidity gap disclosure requirements outweigh the benefit of the incremental and limited information provided to financial statement users. As such, we recommend that the Board work with the SEC to incorporate incremental information within the liquidity gap table into MD&A. This would allow life insurance companies to discuss their unique liquidity risk management strategies and assumptions, which we believe would be more meaningful to financial statement users.

Question 2: For an entity that is not a financial institution, the proposed amendments would require a cash flow obligations table that includes the expected maturities of an entity’s obligations. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

No. However, we believe this table is more appropriate for P&C companies than the liquidity gap table, because they generally use cash flows from operations (e.g., policyholder premiums) to pay obligations as they come due, which is consistent to the Board’s description of a nonfinancial institution in the BC, paragraph 8.

Question 3: The proposed amendments would require information about expected maturities for financial assets and financial liabilities to highlight liquidity risk. Expected maturity is the expected settlement of the instrument resulting from contractual terms (for example, call dates, put dates, maturity dates, and prepayment expectations) rather than an entity’s expected timing of the sale or transfer of the instrument. Do you agree that the term expected maturity is more meaningful than the term contractual maturity in the context of the proposed liquidity risk disclosures? If not, please explain the reasons and suggest an alternative approach.

We do not believe that the definition of expected maturity is more meaningful than the term contractual maturity, given that liabilities that arise from insurance contracts do not have contractual maturity dates. Many life insurance products do not have explicit contractual maturities (e.g., variable and fixed deferred annuity products, universal life-type products, whole life insurance products, etc.) and for those that do (e.g., individual term life) policyholders may have the right to continue the policy past the original term. Therefore, expected liability payments would generally appear to be long and, thus bucketed in the ‘5-years from report date’ and ‘thereafter’ columns. Instead of having a contractual maturity date, life insurance products require actuarial estimates of expected death benefit claims, lapses, surrenders, and other actuarial assumptions affecting the amount and timing of expected cash flows for these policies. It would be more meaningful to have the liquidity gap maturity table reflect these actuarial estimates. This
information could be analogized to the prepayment expectations that a bank would use in showing the expected maturity of loans to consumers. The ED should be revised to allow insurers to use their actuarial estimates in the disclosures rather than contractual maturities. Furthermore, neither expected nor contractual maturities are relevant to an insurer’s management of liquidity risk. Risk management is a much more dynamic and complex process than can be tabulated or narrated in a footnote disclosure to historical financial statements. Therefore, we urge the Board to work with the SEC and other regulators to provide financial statement users with more comparable, but useful information regarding an insurer’s true exposure to liquidity risk, its outlook, and the different ways it manages liquidity risk. As this would include forward-looking assumptions, we recommend moving these discussions into the MD&A.

Question 4: The proposed amendments would require a quantitative disclosure of an entity’s available liquid funds, as discussed in paragraphs 825-10-50-23S through 50-23V. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

Yes. Depending on the level of disaggregation required to populate this table, which is unclear, it could be operationally difficult and costly for some insurers who may use IT systems to capture the data that were not historically scoped into their financial reporting process. For example, if the available liquid funds table required liquid investments at the legal entity level versus the reportable segment level, many insurers would have collect to a vast amount of information in order to prepare this table. Therefore, to minimize operational concerns and implementation costs, we recommend the Board provide insurance entities the flexibility to populate their available liquid funds disclosure at the legal entity level, operating segment, or reportable segment level.

Question 5: For depository institutions, the proposed Update would require a time deposit table that includes the issuances and acquisitions of brokered deposits during the previous four fiscal quarters. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

Yes. Although, similar information is currently being provided to regulators and financial statement users in the MD&A, we believe the auditors will encounter difficulties obtaining comfort over a depository institution’s uninsured deposits as they require complex estimates. This would unnecessarily increase audit costs, because banking regulators currently accept this unaudited estimate.

Question 6: As a preparer, do you feel that the proposed amendments would provide sufficient information for users of your financial statements to develop an understanding of your entity’s exposure to liquidity risk? If not, what other information would better achieve this objective?

No. We do not believe the proposed amendments will provide meaningful or clear information for users of insurance company financial statements as the information requested is not aligned with an insurer’s liquidity management (e.g., management’s ability and intention to reinvest financial assets). We believe that a more focused discussion of liquidity risk and how insurers manage those risks would be more appropriate in the MD&A.

Questions for Users—Liquidity Risk (Questions 7-12) → N/A
Questions for Preparers and Auditors—Interest Rate Risk

Question 13: The interest rate risk disclosures in this proposed Update would require a repricing gap table. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

Yes. As noted in our comprehensive recommendation and responses to liquidity risk questions, we do not believe that this information would represent the business model of P&C companies. P&C companies are not spread focused businesses, as such, asset-liability management is not as integral to measure liquidity risk as it is to a spread focused life insurance company. P&C companies generally use cash flows from operations to pay obligations as they come due. This business model is similar to the Board’s description of a nonfinancial institution in the Basis of Conclusion (BC) paragraph 8. As such, in order to comply with this requirement, P&C companies would have to tailor their systems and financial reporting process to compile information they do not typically use to manage their businesses. To remove this concern, we strongly recommend that P&C companies be excluded from the definition of a financial institution.

As for life insurance companies, our operational concern pertains to the weighted-average yield applicable to the carrying amounts of policyholder reserves in each time interval. Many life insurers have the ability to divide their total policyholder reserves into the predefined time intervals based on the next repricing date, but they often do not know the related crediting interest rates at the report date. This is due to the fact that the crediting interest rates are based on future events (e.g., future market performance of its financial assets). Therefore, to comply with the proposed repricing gap table, life insurance companies would need to disclose information about decisions they have not yet made. This could create discrepancies within the industry. Additionally, the next repricing date could be annually in which case it would push the entire carrying amount of the liability into the current year. We do not believe this information would be meaningful as it would not reflect how a change in interest rates would impact life insurers’ policyholder liabilities. Therefore, we recommend the Board and the SEC partner together to move relevant information within this repricing gap table into the MD&A.

Question 14: The interest rate risk disclosures in this proposed Update would include a sensitivity analysis of net income and shareholders’ equity. Do you foresee any significant operational concerns or constraints in determining the effect of changes in interest rates on net income and shareholders’ equity? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

No. We do not believe the sensitivity analysis would provide meaningful information for a P&C company because typically a P&C company’s loss reserves are undiscounted unless fixed and reasonably determinable. Therefore, the vast majority of their policyholder liabilities are not directly impacted by interest rates.

As for a life insurance company, the interest rate sensitivity analysis table as currently proposed would mislead many financial statement users because of its prohibition to use forward-looking assumptions. Without the ability to incorporate forward-looking information about policyholder behavior and management’s actions the table would not be relevant. To illustrate this point, consider a life insurer’s life insurance policies not carried at fair value. If management does not reflect changes in crediting rates or policyholder behavior, the instantaneous “shock” scenarios would have no impact on policyholder reserves because there is no component of the calculation of the reserves carrying value that would change. For this reason, we recommend the Board and SEC jointly work together to move applicable
information into the MD&A where management’s forward-looking assumptions and risk strategies could be discussed. We believe this would provide more meaningful information to financial statement users.

Question 15: As a preparer, do you feel that the proposed amendments would provide sufficient information for users of your financial statements to understand your entity’s exposure to interest rate risk? If not, what other information would better achieve this objective?

No. The usefulness of the proposed interest rate sensitivity table would be limited for a P&C company. The after-tax net income and shareholders’ equity impact derived from the predefined movement in market interest rates would, for the most part, only represent the effect of fair value changes on a P&C company’s financial assets as their loss reserves are typically undiscounted. Therefore, we recommend that the Board remove these disclosure requirements for P&C companies as they are not consistent with P&C companies’ business models and do not provide useful information about interest rate risk.

As for a life insurer’s interest rate risk, we do not believe the information required accurately reflect an insurer’s exposure to changes in market interest rates. Insurance company asset-liability management is not a static process, it involves multi-scenario modeling that cannot be captured in a historical, point-in-time, simplistic tabular analysis. For life insurance companies, we ask the Board to consider the unique aspects of policyholders’ liabilities and modify the interest sensitivity analysis disclosures so that users can obtain accurate information regarding insurers’ exposure to market interest rate fluctuations.

Questions for Users—Interest Rate Risk (Questions 16- 19) → N/A

Questions for All Respondents
Question 20: The amendments in this proposed Update would apply to all entities. Are there any entities, such as nonpublic entities, that should not be within the scope of this proposed Update? If yes, please identify the entities and explain why.

We are not aware of any entities that should be excluded from the entire scope of the guidance. However, we believe it is inappropriate to define P&C companies as financial institutions. P&C companies are not spread focused businesses, as such, asset-liability management is not as integral to measure liquidity risk as it is to a spread focused life insurance company. P&C companies generally use cash flows from operations to pay obligations as they come due. This business model is similar to the Board’s description of a nonfinancial institution in the BC paragraph 8.

Question 21: Although the proposed amendments do not have an effective date, the Board intends to address the needs of users of financial statements for more information about liquidity risk and interest rate risk. Therefore, the Board will strive to make these proposed amendments effective on a timely basis. How much time do you think stakeholders would require to prepare for and implement the amendments in this proposed Update? Should nonpublic entities be provided with a delayed effective date? If so, how long of a delay should be permitted and why? Are there specific amendments that would require more time to implement than others? If so, please identify which ones and explain why.

In our experience, we believe that these process and system changes would take significant time. We believe that this information would not be auditable in less than 18 months. We also believe that additional training and development would be required for both auditors and finance departments of smaller, nonpublic entities. As such, we recommend providing nonpublic companies with at least a one year delayed effective date.
Question 22: Do you believe that any of the amendments in this proposed Update provide information that overlaps with the SEC's current disclosure requirements for public companies without providing incremental information? If yes, please identify which proposed amendments you believe overlap and discuss whether you believe that the costs in implementing the potentially overlapping amendments outweigh their benefits? Please explain why.

The proposed amendments may require information that overlaps with current SEC disclosure requirements, thus public companies may have information required in the proposed ASU readily available. However, as a nonpublic mutual insurance company, we would like to highlight the fact that the proposed amendments would be new for nonpublic companies, and thus they would require additional time and effort to implement. As such, we recommend providing nonpublic companies with at least a one year delayed effective date.