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Insurance Regulation

*State or Federal
Which Works Best?*

Ratemaking and Product Management (RPM) Seminar
Casualty Actuarial Society
March 16, 2010

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Agenda

- Calls for Change
- Discuss Various Regulatory Framework Proposals
- State Regulatory Perspective
- The Economic Downturn
- The Solution

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Simplicity or Deregulation

- Is the Goal Simplicity or Deregulation?
- Do We Need Change (State to Federal) or Improved Uniformity and Efficiency?
- Property and Casualty Insurers Seeking Freedom from Rate Regulation
- Life Insurance Industry
- EU Carriers – Reinsurance Collateral, US Financial Regulation vs. Solvency I and II
- Globalization of Certain Markets

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State Regulatory Perspective

- Simplicity v. Regulatory Arbitrage
- Accreditation
- Uniformity Where Crucial
 - Financial Statements & Accounting Standards
 - Peer Review thru FAWG
 - SERFF
 - IIPRC
 - NIPR
 - Operational Efficiencies
- Consumer Protection

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State-based Insurance Regulation

- State-based insurance regulation contains a system of checks and balances
- These checks and balances influence
 - The design of regulatory policy
 - The implementation of regulatory policy
- Multiple eyes on a problem means things are less likely to be missed or to be ignored. Peer pressure constrains regulatory forbearance and capture.

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Multistate Coordination

- Multistate coordination and oversight, both bilaterally and through NAIC
- Peer review mechanisms
 - Financial Analysis Division
 - Financial Analysis Working Group
 - Accreditation Program
- Centralized financial reporting/databases with multistate access and analysis tools
- Coordinated development of examination handbook, processes, and automated tools
- Coordinated development of statutory accounting, financial reporting requirements, RBC, holding company regulation, etc.
 - Substantially uniform adoption in the area of solvency regulation because of the accreditation program
- Constant multistate communication/coordinatoin
 - NAIC meetings – task forces, working groups
 - Lead state framework
 - Market Actions Working Group
- Transparency, transparency, transparency

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Regulating Systemic Risk

- Banking and insurance are different!
 - Insurance firms are less likely to present systemic risk
 - AIG problems stemmed from outside the insurance companies
- Insurance companies are owned by a variety of enterprises and could be part of a systemically risky complex institution.

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NAIC Principles

- The NAIC supports initiatives to enhance financial stability where:
 - A system for regulating systemically risky institutions integrates but does not displace state insurance regulation
 - The system ensures effective coordination, collaboration, and communication among the various regulators.
 - Preemption is limited to extraordinary circumstances that present a material risk to the continued solvency of a systemically risky holding company
 - One company in a holding company structure should not be compromised for the benefit of another company in another sector

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NAIC Modernization Efforts Over the Years

- **Producer Licensing**
 - National Insurance Producer Registry
 - 47 states are certified as reciprocal under GLBA
 - Pursuing greater uniformity
- **System for Electronic Rate and Form Filing (SERFF)**
 - In 2008 over 550,000 filings were processed using SERFF; over 2800 insurers use SERFF
 - It is estimated that 90% of all filings are filed through SERFF;
 - Average filing turnaround time for L&H filings is under 42 days; for P&C filings under 35 days;
- **Interstate compact for regulation of life and annuity products**
 - 36 states
 - more than 50 uniform standards in the individual life and annuity product lines, providing greater flexibility to companies in their product filing options.
- **Market conduct**
 - Market analysis
 - Interstate collaboration – the market actions working group (MAWG)

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US Insurance and Global Markets

(Millions of U.S. Dollars)

1	United States	\$1,546,860	35.33%
2	United Kingdom	\$463,686	10.59%
3	Japan	\$424,832	9.70%
4	France	\$268,900	6.14%
5	Germany	\$222,825	5.09%
6	Italy	\$142,328	3.25%
	The Rest	\$1,308,498	29.89%
	Total	\$4,377,929	100.00%

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How States Compare

- 3 of the Top 10 Jurisdictions
- 7 of the Top 20 Jurisdictions
- 10 of the Top 25 Jurisdictions
- 13 of the Top 30 Jurisdictions
- 21 of the Top 40 Jurisdictions
- 28 of the Top 50 Jurisdictions

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Global Competition (US v. EU)

<ul style="list-style-type: none"> • US • Accreditation-50 States • One language • 50 States, DC & Terr. • 304 Million People • One Currency 	<ul style="list-style-type: none"> • EU • 23 Languages • 27 Countries (Not All) • 493 Million People • Euros & > 10 Others
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The Economic Downturn

- Insurers have weathered the storm relatively better than other financial services providers – WHY??
 - Picky state laws regulating insurers' investment activities
 - Wealth of financial information regularly provided to regulators
 - Active cross-border information sharing
 - Sound financial monitoring tools (IRIS & RBC)

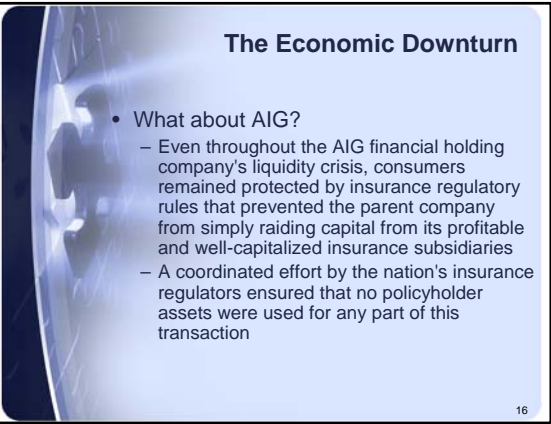
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The Economic Downturn

- What about AIG?
 - AIG is a financial services conglomerate
 - American International Group, Inc., is a financial holding company that owns 71 U.S.-based insurance entities and 176 other financial services companies throughout the world
 - The problem lies with the AIG financial holding company that is subject to federal regulatory oversight by the U.S. Office of Thrift Supervision (OTS).

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The Economic Downturn

- What about AIG?
 - Even throughout the AIG financial holding company's liquidity crisis, consumers remained protected by insurance regulatory rules that prevented the parent company from simply raiding capital from its profitable and well-capitalized insurance subsidiaries
 - A coordinated effort by the nation's insurance regulators ensured that no policyholder assets were used for any part of this transaction

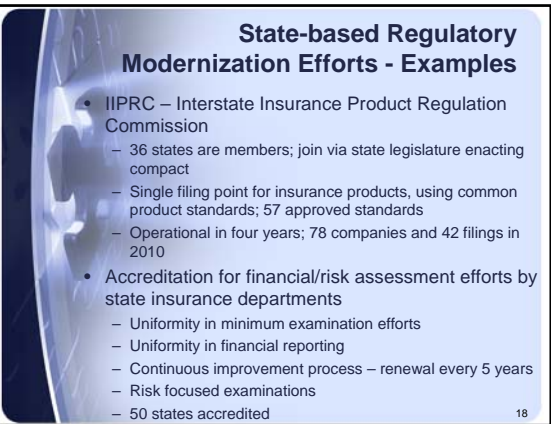
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The Solution

- Unregulated/loosely regulated financial service markets – transparency and federal regulation comparable to insurance regulation.
- State-based solutions for insurance regulation modernization:
 - Compacts/IIPRC
 - Accreditation
 - Collaboration with Federal Regulators
 - Solvency Modernization

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State-based Regulatory Modernization Efforts - Examples

- IIPRC – Interstate Insurance Product Regulation Commission
 - 36 states are members; join via state legislature enacting compact
 - Single filing point for insurance products, using common product standards; 57 approved standards
 - Operational in four years; 78 companies and 42 filings in 2010
- Accreditation for financial/risk assessment efforts by state insurance departments
 - Uniformity in minimum examination efforts
 - Uniformity in financial reporting
 - Continuous improvement process – renewal every 5 years
 - Risk focused examinations
 - 50 states accredited

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Solvency Modernization Initiative(SMI)

- US regulators have developed a detailed and uniform financial regulatory system over its years of existence.
- In the early 1990s, the NAIC's Solvency Policing Agenda resulted in a number of major changes to financial regulation (e.g., RBC, accreditation, FAST system, FAWG and FAD)
- Continuous improvement over the past 20 years have resulted in many modifications (e.g., model audit rule, risk-focused exams, uniform statutory accounting model)
- Today, global and national developments call for another comprehensive review.

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SMI Focus Areas

- Focus areas:
 - International Accounting (Statutory Accounting and Reporting)
 - Insurance Valuation (Principle-Based Reserving)
 - Capital Requirements (Risk-Based Capital)
 - Group Solvency Issues (including Group Capital Requirements)
 - Reinsurance (Adopted Reinsurance Modernization Framework)
- Other Considerations:
 - Enterprise risk management
 - Corporate governance

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Solvency Modernization Initiative (SMI)

- Describe the U.S. system based on a coherent set of principles.
- Examine international developments and their potential use in U.S. insurance regulation.
 - The Basel II international capital framework for banks and implementation in the U.S.;
 - Solvency work by the International Association of Insurance Supervisors (IAIS);
 - Solvency proposals in place or under development in other jurisdictions, including Australia, Canada, Switzerland and the EU Solvency II;
 - International accounting standards being developed by the International Accounting Standards Board (IASB).
- Critically review the entire solvency regulation framework in the U.S.
 - Keep what is working well and add requirements as needed.
 - Modify or delete requirements that are not working well.

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