

Testimony of the  
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National Association of Insurance Commissioners

Before the  
Subcommittee on Housing and Insurance  
Committee on Financial Services  
United States House of Representatives

Regarding:

The Impact of International Regulatory Standards on the  
Competitiveness of U.S. Insurers

June 13, 2013

## **Introduction**

Chairman Neugebauer, Ranking Member Capuano, and members of the Subcommittee, thank you for the opportunity to testify today on behalf of the National Association of Insurance Commissioners (NAIC).

My name is Ben Nelson, and I serve as the Chief Executive Officer of the NAIC. The NAIC is the United States standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia, and five U.S. territories. Through the NAIC, we establish standards and best practices, conduct peer review, and coordinate our regulatory oversight. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

The NAIC and its members have long been committed to providing leadership on a wide range of global insurance issues and activities, with a focus on ensuring policyholder protections and maintaining stable insurance markets. As insurance markets become more global, U.S. state insurance regulators are extensively engaged with their international counterparts in developing the elements of a stronger international insurance regulatory framework. We have encouraged an international focus on promoting and supporting the development of best practices in emerging markets, and are also working to ensure that global standard-setting is compatible with our strong and effective state-based system. International developments at the Financial Stability Board (FSB) and the International Association of Insurance Supervisors (IAIS) have the potential to directly impact U.S. insurance regulation and U.S. insurers, and, therefore, U.S. consumers. The NAIC and state regulators have an obligation to be engaged and participate in these developments, in partnership with the federal government when appropriate.

Today, I will provide the subcommittee with an overview of the NAIC's involvement in international discussions and key international regulatory developments. Specifically, my testimony will focus on four major areas: 1) the development of a Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame); 2) the identification of global systemically important insurers; (3) the U.S.-European Union Dialogue Project; and (4) international trade. In addition, I will discuss our interaction with the U.S. Treasury Department's Federal Insurance Office (FIO) with regard to international insurance activities.

## **Supervision of Internationally Active Insurance Groups**

U.S. state insurance regulators and the NAIC have been active in the development of ComFrame. This project, conducted through the IAIS, aims to assist supervisors in performing more effective group-wide supervision of internationally active insurance groups, foster greater cooperation and coordination among supervisors around the world, and foster convergence of supervisory approaches.

We support the original goals of ComFrame and continue to believe there is merit in developing a framework for greater coordination and cooperation among different jurisdictions to achieve more effective and more efficient regulation. However, the current scope and prescriptive nature of ComFrame overshoots those goals, and over complicates what is necessary for effective cross-border supervision. In our view, ComFrame should support and enhance the work of

international supervisory colleges<sup>1</sup>, which serve as the actual vehicles to achieve these objectives. State insurance regulators have held, or have scheduled to hold, supervisory colleges for all 15 U.S. firms that meet the current IAIS definition of an internationally active insurance group. Key state regulators have also participated as involved supervisors in colleges for international groups based overseas that do significant insurance business in the U.S.

While we continue to work within the IAIS to focus the ComFrame effort on developing a common set of principles for effective international group supervision, U.S. state regulators remain wary of this project's tendency towards "mission creep" and the accumulation of overly prescriptive requirements, and a one-size-fits-all approach that could impose new burdens on U.S. companies and consumers with little, if any, benefit. Given the different regulatory approaches and structures among IAIS members and the differences among internationally active groups, ComFrame must be a dynamic and flexible framework focused on regulatory collaboration and achieving similar supervisory outcomes.

The NAIC and its members are working to ensure that the proposed standards under discussion are compatible with our U.S. state-based system and make sense for U.S. insurers. Of paramount importance is ensuring that implementation of ComFrame does not undermine our strong solvency standards for U.S. insurance entities. Ensuring that each subsidiary of a complex group engaged in insurance is solvent and appropriately capitalized is a cornerstone of our system and one reason insurers weathered the financial crisis so well. Certainly there is potential for a variety of benefits from ComFrame if done correctly, but we have no intention of implementing those elements that would be impractical and counterproductive if imposed here in the U.S.

As we provide input to the IAIS and other international projects, we have to be mindful of our regulatory and legal structure at home. In the U.S., we have functional regulation with some areas of consolidated supervision. We are concerned that related discussions on the need for a Global Capital Standard for insurance could push for a bank-like approach to capital that is not appropriate. On the Group Supervision front, we remain skeptical of those that believe that one set of eyes can do better than multiple sets – our experience with the financial crisis suggests otherwise. With this in mind, we urge Congress to continue to be wary of any international prescriptions seeking to impose new standards on the United States.

### **Identification of Global Systemically Important Insurers**

In the aftermath of the financial crisis, regulators in the U.S. and around the world increasingly focused on identifying systemic risks to the financial system. As part of this effort, work has been underway to designate domestic and global systemically important insurers (G-SII's). U.S. state insurance regulators and the NAIC have had substantial involvement in this process through representation on the U.S. Financial Stability Oversight Council (FSOC) by Missouri Insurance Director John Huff and on the IAIS Financial Stability Committee by Connecticut Insurance Commissioner Thomas Leonardi and NAIC staff, as well as other state regulators as part of the home jurisdiction consultation process.

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<sup>1</sup> The International Association of Insurance Supervisors (IAIS) defines a supervisory college as "a forum for cooperation and communication between the involved supervisors established for the fundamental purpose of facilitating the effectiveness of supervision of entities which belong to an insurance group; facilitating both the supervision of the group as a whole on a group-wide basis and improving the legal entity supervision of the entities within the insurance group."

It is the view of state insurance regulators that allowing insurers to engage in activities that make them systemic is not in the interests of policyholders. To the extent that an insurer engages in activities that could result in a systemically important financial institution (SIFI) or G-SII designation, U.S. and international regulators should work diligently and collaboratively to address the sources of systemic risk with the goal of reducing the potential systemic impact of the insurer to such a degree that it is no longer systemic. With that in mind, we continue to examine the scope of our authorities and resources to ensure that systemic risk does not emanate from activities or entities within our purview.

We have concerns that the creation of two tiers of companies, where some are perceived to be safer than others, could reduce market discipline, create competitive distortions, and encourage undesirable consolidation and concentration in the insurance sector. We believe this could lead to creation of the “too big to fail” companies that both FSOC and IAIS G-SII initiatives are aimed at avoiding. Indeed, subsequent to recent announcements that the FSOC issued proposed designations of certain insurers, Moody’s indicated that such designation was a “credit positive” event, and that the credit benefits of a designation outweigh the drawbacks.

The threshold that companies must meet to be designated as a SIFI domestically or a G-SII abroad is rightfully designed to be steep. In the United States, FSOC may designate a non-bank financial company for heightened supervision by the Federal Reserve if the company could pose a threat to the financial stability to the United States, which the Council has defined as “the potential for impairment of financial intermediation or financial market functioning that would be sufficiently severe to inflict significant damage on the broader economy.” Internationally, the determination standard for identifying global systemic insurers is comparably high, requiring a firm’s failure to cause significant disruption to the wider financial system and economic activity. While it is entirely appropriate to identify insurers that pose clear risks to the financial system at home or abroad, given the potential for negative market implications, such designation should be the product of a rigorous analysis that reflects a thorough understanding of the insurance business model and regulatory system, and demonstrates that these high standards are met.

Finally, both processes should be aligned with appropriate deference to domestic authorities. It is the view of the U.S. insurance regulators that the threshold for being designated a threat to global financial stability should be higher than the threshold for being designated a domestic threat to financial stability. As such, the G-SII list should not contain any U.S. insurers that have not otherwise been designated SIFI’s by FSOC. This would also ensure that the impact of any designation of a U.S. firm is rooted in clear legal authority and process.

### **U.S.-European Union Dialogue**

In addition to our work in the IAIS, U.S. state insurance regulators have also been actively involved in the U.S.-EU Insurance Dialogue Project. Since January of 2012, the NAIC, FIO, the European Commission, and European Insurance and Occupational Pensions Authority have been engaged in a more extensive dialogue process to enhance both sides’ understanding of our unique solvency oversight systems and explore ways to increase cooperation.

Last December, the Project’s Steering Committee issued a joint report along with a separate paper outlining a set of common objectives and a series of initiatives designed to enhance insurance regulatory cooperation internationally. These initiatives focus on important areas such

as group supervision and the coordination of international supervisory colleges, as well as enhancements to data collection and analysis, independent third party reviews, and the conduct of on-site and off-site examinations. The project builds on the on-going U.S.-EU Insurance Dialogue, which has been in place as a vehicle for regulator-to-regulator exchange for more than a decade.

The goal of this work is to explore areas of potential alignment and opportunities for greater collaboration between the two systems over the long term. Significant progress has been made, and we are engaged in advancing common objectives and initiatives over the next five years. Many of these initiatives are already underway or under consideration within the NAIC process at one or more committees or working groups. While much work lies ahead, U.S. state insurance regulators are working diligently to enhance this transatlantic relationship.

### **International Trade**

Next, I would like to focus on our involvement in international trade issues. The insurance sector plays a significant role in promoting economic development, and we must maintain a level playing field here and abroad in order to create and protect jobs. State regulators are keenly aware of the importance of international trade and trade agreements for economic development while ensuring consumer protection for our domestic constituents.

As the Office of the United States Trade Representative (USTR) negotiates agreements, such as the ongoing Trans Pacific Partnership and the upcoming Transatlantic Trade and Investment Partnership, and seeks improved market access for U.S. insurers, the NAIC will continue to provide technical insurance expertise to the USTR. Our partnership with USTR dates back to the early 1990s when the North American Free Trade Agreement (NAFTA) and General Agreement on Trade in Services (GATS) were negotiated.

Throughout our two decade relationship with the USTR, State regulators and the NAIC have sought to promote stable practices emphasizing the successful track record of the U.S. market. We illustrate to our trading partners the importance of insurance to our economy in terms of jobs, economic output, and risk mitigation for consumers.

Moving forward, the NAIC will continue to assist in the efforts of the Federal government to open and maintain competitive, transparent, well-regulated markets; enhance the stability of regulatory practices among trading partners; eliminate unnecessary barriers to U.S. trade commitments; and enhance consumer protection.

### **Interaction with FIO in International Insurance Activities**

In many of these international discussions, we have been working with the U.S. Treasury Department's Federal Insurance Office (FIO). The NAIC has long believed that the FIO can supplement and enhance existing efforts of the NAIC and the U.S. insurance regulators and add another federal voice to international discussions regarding insurance issues. However, the FIO has no statutory regulatory or quasi regulatory authority and does not speak for U.S. insurance regulators. Recognizing its narrow yet potentially beneficial role, the NAIC supported the creation of the FIO during the debate over the Dodd-Frank Act.

While the Treasury Department and the U.S. insurance regulators may not agree on every issue, we should always collaborate, seek common ground that is consistent with the interests of U.S. consumers and industry, and, whenever possible, engage the international community in a united fashion. In this regard, we would expect to give a certain amount of deference to the Treasury Department in international discussions involving issues that do not implicate our regulation of the U.S. insurance industry. However, we expect the Treasury Department to give similar deference to, and support the views of, the regulators in forums like the IAIS that focus almost exclusively on regulatory issues that have little or no impact on FIO's authority or responsibilities. Moreover, it is inappropriate for FIO or any other non-regulator to seek to participate in supervisory colleges, which are vehicles to discuss supervision of specific companies, without an invitation from the regulators.

The NAIC and U.S. insurance regulators are committed to work through any disagreements that may arise with the Treasury Department so we can serve our respective roles and more effectively represent the best interests of U.S. industry and consumers. The Dodd-Frank Act made clear a separate non-regulatory role for FIO and supported the state-based regulatory system.

### **Conclusion**

U.S. insurance regulators have a strong track record of effective collaboration and supervision, and the NAIC is committed to coordinating with our international counterparts to help ensure open, competitive, and stable markets around the world. It is critical that we promote a level playing field across the globe through strong regulatory systems while recognizing that there will continue to be different cultural, legal, and operational differences in regulatory regimes around the world. Uniform global standards are not necessary to achieve compatibility and equivalent results. Congress has delegated insurance regulatory authority to the states so we have a continuing obligation to engage internationally in those areas that impact the U.S. state-based system, companies, and consumers. While we appreciate international developments and standards, and consider them as we continually improve our system, we should not toss aside our time-tested state-based system in pursuit of untested and overly burdensome approaches just for the sake of diplomacy and collegiality.

Our state-based system in the U.S. has a strong track record of evolving to meet the challenges posed by dynamic markets, and we continue to believe that well-regulated markets, both here and abroad, make for well-protected policyholders.

Thank you again for the opportunity to be here on behalf of the NAIC, and I look forward to your questions.