Global Capital Standards: Implications for the U.S.

Thank you for that kind introduction.

At the heart of today's discussion are two important questions, and perhaps a few others. How much should insurance regulators rely on capital as the be all and end all of regulatory tools, and would development of a global insurance capital standard leave policyholders or the financial system any safer, and if so, at what cost? I hope we can explore those fundamental issues today, but let me start with where things stand in the U.S. America's insurance regulatory framework was responsible for the protection of insurance consumers and companies in the U.S. during the financial crisis, and has only improved in the last six years. We have increased our dialogue with foreign regulators including our participation in Supervisory Colleges; gained a better understanding of how other financial companies are – or aren't – regulated; and recently completed the Solvency Modernization Initiative. All of which strengthen our system while preserving the elements that fundamentally work well. Today, we are better equipped to identify and reign in activities that could put policyholders and the financial system more at risk than ever before.

Capital is an important part of our system. Following a number of insolvencies in the 1980s and early 1990s, we set to work on building a risk-based-capital system and improving the financial reporting and analysis that go with it. We ensured that all legal entities within the group are separately capitalized so that there are assets to pay policyholder claims, regardless of what might be happening elsewhere within the group. This legal entity approach is like the multiple bulkheads in a ship, ensuring that losses or damage in one area do not spill over to others, helping keep the entire enterprise afloat. This was critical to our success during the crisis, particularly when insurers were connected to other activities that in some cases, like credit default swap, required no capital at all.

So we understand the importance of capital, but are wary that fixating on capital is a mistake. I come to this discussion on global group capital standards with a healthy dose of skepticism, and insistence that any changes to the U.S. regulatory structure are carefully reviewed and implemented pragmatically. American consumers and the financial structure as a whole demand and deserve nothing less.

That's not to say that I, or the NAIC as a body, oppose a global capital standard. As we have taken steps to expand our group supervision and holding company authorities, it makes sense to examine whether assessing the capital needs of the broader group is a necessary complement to our current approach. Nevertheless, there are core considerations that we must work through before advancing any new proposal and what is useful within our system may not mirror what other jurisdictions feel is necessary.

As I asked at the outset, will a global capital standard for insurers make policyholders or the financial system more secure? The answer of course is not simple at all. A global insurance capital standard alone will not protect any one company or the broader economy, just as the existence of Basel banking standards did not prevent hundreds of banks from failing during the crisis. Moreover, it could cause harm if overly burdensome requirements inhibit product offerings and development, raise prices for consumers, add layers of regulation or otherwise discourages appropriate risk management.

I do see value in the IAIS working to ensure that all markets – particularly the emerging markets that represent the future growth centers for our industry – have sufficient capital regimes in place, and providing a measure of consistency across the globe. Of course, we need to make sure that foreign firms are meeting the regulatory benchmarks in the jurisdiction where they sell policies, and that policyholders are protected just as they would be by a domestic insurer. We also must also stand vigilant that any standard does not disadvantage U.S. firms operating in foreign markets.

I also am concerned with the process at the IAIS for development of a global capital standard. Any international standard should not favor one regulatory approach over another. Instead, it should represent the best outcomes that solid regulations provide, and leave it to individual jurisdictions to develop the best way forward. Given the differences in regulatory structure, authorities, accounting, and legal environments, a single uniform standard is unlikely, and I would argue unnecessary if we can all work toward a high degree of consistency while preserving the diversity in regulation that makes for a stronger more resilient marketplace.

It's critical to remember that if a global standard is developed, it carries only as much weight and value as the regulators around the world are willing to give it. Just as the IAIS is shutting down open meetings and limiting stakeholder and observer engagement, they are also seeking buy-in from regulators. NAIC meetings aren't always pretty, and our members will often disagree – as they should – on issues of regulatory policy. But that "airing of the grievances" in a public forum gives us confidence that when we reach a conclusion, the finished product is in the best interest of the insurance marketplace.

My last concern remains with the timing of an international capital standard. Any timeline should be driven by the regulators – the IAIS members – based on resources available to deliver high-quality results. For example, how can we have a global capital standard before we have a global accounting system? What mechanisms are in place – or need to be created – to reconcile the differences? NAIC members have an obligation to be at the table internationally to help answer these questions, but right now, there are far more of these questions than answers.

I look forward to today's discussion, and hope we can shed some light on the necessity, process and timing of a global capital standard.