

Testimony of Lee Covington
Director of Insurance
State of Ohio

Before the
Subcommittee on Finance and Hazardous Materials
Committee on Commerce
United States House of Representatives

Regarding
State Insurance Regulatory Modernization and
Implementation of the Gramm-Leach-Bliley Act

September 19, 2000

Summary of Testimony by Lee Covington

- As described by NAIC President George Nichols at the Subcommittee’s July hearing, the National Association of Insurance Commissioners (NAIC) and State insurance regulators are on track to implement all provisions of the Gramm-Leach-Bliley Act (GLBA) as intended by Congress:
 - a) We are actively coordinating and cooperating with Federal functional regulators through cooperation agreements, personal contacts, and information exchanges among State and Federal supervision staff.
 - b) We have developed model privacy rules similar to the Federal privacy regulations that can be quickly adopted by States to assure compliance with GLBA.
 - c) We are establishing a one-stop national licensing system for insurance agents and brokers that will fully satisfy the NARAB provisions in GLBA by achieving reciprocity among States while we develop and implement a uniform 50-state system.
- The NAIC is spearheading a bold set of national initiatives, as outlined in the “Statement of Intent—The Future of Insurance Regulation” and signed by all State Insurance Commissioners, that will move State insurance regulation beyond GLBA by achieving uniformity and greater efficiency for agent licensing, establishing national treatment of companies, speeding up the process for introducing insurance products to market, and facilitating e-commerce.
- Ohio is leading the way in modernizing State insurance regulation by being the first State to adopt reciprocity for agent licensing, implementing a state-of-the-art internet licensing system, piloting the National Insurance Producer Registry allowing one-stop licensing for non-resident agents, adopting regulations to speed the time for insurance product approvals, and chairing NAIC committees with the goal of facilitating the use of e-commerce and improving the State-based insurance product approval process.

Testimony of Lee Covington

Ohio Director of Insurance

Introduction

Chairman Oxley and members of the Subcommittee, my name is Lee Covington. I am the Director of Insurance in state of Ohio and serve as Chair of the National Association of Insurance Commissioners' (NAIC) Regulatory Re-engineering Task Force, the Electronic Commerce & Regulation Working Group, and the Improvements in State-Based Systems Subgroup of the Speed to Market Working Group.

Thank you for inviting me to testify regarding the efforts of Ohio and other State insurance regulators, in our own States and through our work as members of the NAIC, to implement the Gramm-Leach-Bliley Act (GLBA) and modernize State insurance regulation. I am especially pleased to be here because Ohio is a leading State in modernizing our regulatory system to fully meet the expectations of insurance consumers and the financial services industry.

Mr. Chairman and members of the Committee, I thank you for your leadership in working to enact GLBA in the face of changing consumer demands and a financial services industry marked by globalization, convergence, consolidation, and technological innovation. I join my colleagues in thanking you and this committee for your support of functional regulation of insurance by the States when enacting GLBA, for your continued support of State insurance regulation, and for your support of our efforts to make real progress in our regulatory modernization initiatives.

During the Subcommittee's hearing on July 20, 2000, Chairman Oxley noted that insurance commissioners, through their "Statement of Intent", "have demonstrated now that they can "talk the talk"; if they can also "walk the walk", then insurance consumers and producers can fully benefit from uniformity without the need for a new federal system." Chairman Oxley also requested an update "to assess what progress has been made and whether there is a sufficient continuing commitment to uniformity." Further, Chairman Oxley "hope[d] that the NAIC

working groups [would] not only be able to come up with specific proposals for achieving their goals, but to attach specific time frames to implement those proposals in the 50 States.” I am excited to report that State insurance regulators remain strongly committed to our modernization initiatives with unprecedented consensus, and after a series of meetings leading to our most recent National Meeting, we have accomplished just what you had hoped to see—specific proposals with specific time frames. I applaud the outstanding leadership of NAIC President George Nichols over the past 10 months and the intense work and commitment of each State insurance commissioner as we have moved forward on each of our initiatives.

Today, I would like to make three points about where State regulators stand in implementing GLBA and achieving our modernization goals –

- First, the NAIC and State insurance regulators are on track to implement all provisions of GLBA, and move beyond its requirements with our own plan to achieve national uniformity and efficiency for agent licensing.
- Second, consistent with the “Statement of Intent—The Future of Insurance Regulation” signed by all state Insurance Commissioners in March of this year, the NAIC and State regulators are working with the insurance industry and consumers on several fronts to develop specific programs with specific time frames for implementation that will substantially improve the insurance supervision process while creating regulatory efficiencies and reducing costs for insurance companies and agents.
- Third, I am proud to report that our experience in Ohio provides a good example of the substantial progress being made toward modernizing State insurance regulation.

State Regulators Are on Track Implementing GLBA

At the Subcommittee’s hearing on July 20, 2000, NAIC President George Nichols gave a detailed summary of the steps being taken by NAIC and State regulators to implement GLBA. He concluded: “The NAIC and State insurance regulators are well on the way to implementing

the provisions of GLBA as intended by Congress.” His statement remains true. The NAIC completed several additional steps of our GLBA implementation at meetings held in Kansas City and Dallas after President Nichols testified.

My testimony today provides an update concerning State regulatory efforts to implement the three basic GLBA mandates identified by President Nichols –

- a) Coordinating and cooperating with Federal functional regulatory agencies that supervise banks and securities firms;
- b) Issuing privacy rules to protect the non-public financial information given by consumers to insurance providers; and
- c) Establishing a national licensing system for insurance agents and brokers in order to avoid the creation of the National Association of Registered Agents and Brokers (NARAB).

I will also update you on two additional areas – national treatment of insurers and speeding insurance products to market – where State regulators are moving beyond the requirements of GLBA to modernize our regulatory system.

Cooperating with Federal Regulators under GLBA

The NAIC continues to believe that establishing sound working relationships with Federal regulators is absolutely essential for State insurance departments under GLBA. Long-standing efforts to work closely with our Federal counterparts are now consolidated under the NAIC’s Coordinating with Federal Regulators Working Group, which has been given broad responsibility to stimulate cooperation at all levels.

The NAIC’s first priority for establishing regulatory cooperation is to negotiate and sign written agreements between Federal and State agencies laying out the ground rules for sharing

information and keeping it confidential when necessary. When signed by individual State insurance departments and Federal agencies, these comprehensive agreements will permit information to be shared regarding financial condition, market conduct, and regulatory enforcement matters. At present, NAIC is negotiating model regulatory cooperation agreements with Federal banking agencies as follows –

Federal Reserve Board – After four months of joint effort, NAIC has recently received the latest version of a draft agreement from the Federal Reserve staff. This agreement was distributed last week to members of the Coordinating with Federal Regulators Working Group for review and comment. We expect to reach final agreement on a model by the end of the year.

Office of Thrift Supervision – NAIC approved a comprehensive model regulatory agreement with OTS in June of this year. So far, the agreement has been signed by 23 States. This number will rise as more States direct their attention to completing Federal cooperation agreements.

Comptroller of the Currency – The OCC says it will soon deliver to NAIC a comprehensive draft agreement based upon the OTS model. When NAIC receives it, we will distribute it to Working Group members for review and comment. Currently, 28 States have signed a more narrow consumer complaint sharing agreement with OCC that was approved by NAIC in 1999.

Federal Deposit Insurance Corporation – FDIC is working on a draft agreement, and will be sending it to NAIC in the near future.

The second priority for effective cooperation is to establish personal contacts at Federal agencies that will foster open communication, mutual understanding, and practical cooperation on monitoring and enforcement matters. The process of establishing such personal contacts between State and Federal regulators is going very well. While we have good initial working relationships with all the banking regulators, our contacts with the Federal Reserve and OCC are

the most advanced due to the immediate demands of handling the Citigroup merger and increased insurance activities by national banks.

Relations with the OCC are a good example of how we are proceeding. During the past year, the Coordinating with Federal Regulators Working Group conducted a series of day-long meetings with senior OCC supervision officials and State insurance experts to exchange views and explore general supervision methods. Now, relations are moving forward to resolving the important details of developing examination procedures that address proper supervision of insurance activities by national banks. Through these efforts and continue cooperation and communication, we expect to develop an efficient and effective framework for implementing functional regulation as required by GLBA. We hope to avoid Federal preemption of State insurance laws wherever possible. NAIC expects this natural evolution from general policy discussions to coordinating supervision details will serve as the model for establishing sound working relationships with each of the Federal banking agencies during the coming year.

Meeting GLBA Consumer Privacy Requirements

Members of the NAIC have been discussing and addressing the privacy of personal information, including health information, for more than 20 years. In 1980, the NAIC adopted the Insurance Information and Privacy Protection Model Act, which generally requires insurers to receive authorization from individuals (“opt-in”) to disclose personal information. In September 1998, NAIC adopted the Health Information Privacy Model Act because of the special issues surrounding health information. This model treats personal health information as a different type of information that receives a higher level of privacy protection. NAIC records indicate that 17 States have adopted all or part of the 1980 model, while the 1998 health model has not yet been adopted by any State. The NAIC believes State privacy regulations based upon the 1980 and 1998 NAIC models will exceed GLBA requirements, which means they will remain in force under Section 507 of that law.

To meet the recent challenge of specific GLBA privacy requirements, the NAIC’s Privacy Issues Working Group moved swiftly to construct model insurance consumer privacy regulations that

will serve as guidance for States that do not presently have regulations satisfying the Title V privacy provisions in GLBA. The purpose of these regulations is to help State insurance authorities comply with the minimum requirements of GLBA quickly while State Insurance Commissioners consider whether additional privacy protections are needed across-the-board for all consumers of financial services, including insurance.

After six months of public comment and hearings on four separate drafts, the Working Group approved a final model privacy regulation last week at the NAIC's Dallas National Meeting. Upon approval by the full NAIC membership, which is expected during the next month, this model will move to the States for consideration. States adopting this model will be assured that they meet the minimum requirements of GLBA.

In drafting the model regulation, the Working Group sought to strike a good overall balance between achieving uniformity with Federal privacy rules and adequately protecting personal information more commonly associated with insurance products. The NAIC model also tracks the November 13, 2000, effective date and July 1, 2001, compliance deadline set forth in the Federal regulations.

Some departures from the Federal rules were necessary to reflect the special nature of the insurance business and its impact on consumers –

1. In the NAIC model regulation, “consumers” include not only individuals who have a direct relationship with an insurer, but also other individuals such as claimants, beneficiaries, and persons entitled to coverage under group plans, employee benefit plans, and workers’ compensation plans.
2. Because insurance providers typically collect much greater amounts of health information than banks, the NAIC model includes provisions that protect personal health information. The health provisions of the model regulation give health information a higher level of privacy protection than financial information receives under GLBA. In general, insurers are prohibited from sharing protected health information with any other party – affiliate

or non-affiliate – without the express consent of the consumer to which the information applies (opt in). The 1980 NAIC Model adopted by 17 states contains this same general rule, and therefore, insurers in those states are already complying with these provisions. Finally, to promote uniformity and implementation of privacy protections, the health provisions of the draft model regulation will not apply to insurers who are in compliance with the health information privacy regulations promulgated by the Department of Health and Human Services (HHS) pursuant to the Health Insurance Portability and Accountability Act (HIPAA).

Satisfying the NARAB Provisions in GLBA

Following passage of GLBA, the NAIC moved quickly to amend its Producer Licensing Model Act to comply fully with the NARAB provisions in GLBA, and earlier this month, the NAIC launched a pilot of the National Insurance Producer Registry (NIPR). The model act is the vehicle for States to satisfy the GLBA statutory requirements because it fully implements the requirements for licensing reciprocity and uniformity among States. Adoption of the model by a majority of States by November 2002 will assure that NARAB will not be created. Although our immediate goal is minimum compliance with GLBA, our ultimate goal is for all 50 States to be operating under a national system of unified standards and procedures.

The NAIC is taking several additional steps to improve agent licensing. In partnership with the National Insurance Producer Registry (NIPR), a non-profit affiliate of the NAIC, we have been aggressively investing over the past three years in modernizing our technical infrastructure to develop a more centralized producer licensing processing center. As stated previously, earlier this month, NIPR began a pilot project with four states participating, including Ohio, and we expect to have all states operational in 2001. Through NIPR, non-resident agents will be eligible to receive a license on a reciprocal basis within 24 hours of submitting an electronic application.

At present, the NAIC maintains a regulatory network and centralized database of 2.6 million of the Nation's 3 million producers. This information is available to regulators and insurance

companies over the Internet, and is updated daily by automated processes at the State insurance departments.

Currently, 32 States are online with the Producer Database and the target is to have all 50 States contributing to PDB between December 2000 and June 2001. Because PDB is a mirror of the State licensing database, NIPR is creating a single system to automatically process appointments, terminations, and uniform non-resident license applications on behalf of individual State insurance departments against data in PDB within 24 hours of receiving the electronic data from an insurance company or producer. Approximately 110,000 producer appointments and terminations are being processed by 24 States through NIPR monthly right now, and we expect to have the entire system operational and all 50 States participating in 2001.

The next key step in this process will be the implementation of a single electronic licensing application. These system improvements will bring about regulatory efficiencies that far exceed the expectations in NARAB and set the stage for national uniformity.

Going Beyond GLBA and Modernizing Regulation– National Treatment of Insurers

One key area where State regulators are moving beyond the requirements of GLBA is national treatment of insurers doing business in multiple jurisdictions. This year, the NAIC established the National Treatment of Companies Working Group, and gave it responsibility for identifying regulatory procedures that will treat eligible insurance companies the same across the Nation. One such procedure involves the licensing process for an insurer to obtain a certificate of authority to conduct business in a State. Already, 29 states are participating in the NAIC's Uniform Certificate of Authority Application (UCAA), and one more is in transition. The Working Group's goal is to have all 50 states and the District of Columbia using the UCAA by December 2000.

Another goal is standardizing the licensing review process. While the UCAA provides a uniform application, the Working Group is looking to expand this effort to also include standardized review criteria nationwide. NAIC plans to develop a streamlined operating structure that would

give certain companies “national treatment” for regulatory procedures related to company licensing, solvency monitoring, holding company supervision, approval of mergers and acquisitions, market conduct reviews, and corporate re-organizations.

At NAIC’s National Meeting in Dallas last week, the National Treatment of Companies Working Group discussed these regulatory efficiency goals, and set forth a timeline for achieving them in four progressive steps –

1. Obtain commitments from all NAIC members to participate in the ALERT program, using the UCAA, by December 2000, and to achieve active participation by all NAIC members by June 2001. ALERT stands for “Accelerated License Evaluation Review Techniques”, a program that streamlines regulation by promoting the single license application process, including the application form and review timelines, which is accepted in all participating States.
2. Develop “best practices” for reviewing significant holding company transactions and company licensing applications by December 2000 and June 2001, respectively, and encourage all States and the District of Columbia to administer such reviews on a consistent and uniform basis.
3. Implement the national treatment process through a memorandum agreement between June 2001 and June 2002, and continue to examine whether additional legislative action is need to fully implement the national treatment initiative.
4. Develop enabling State legislation, if necessary, to provide state insurance regulators with the legal authority to implement a national treatment system by June 2003.

The Working Group also discussed possible legal options for implementing national treatment. Using a model law, memorandum agreement, interstate compact, and Federal involvement were all considered. The use of a memorandum of understanding was considered to be an appropriate vehicle for accomplishing the initial implementation of the national treatment process in Goal 3. For the long-term, an interstate compact was considered as a possible vehicle for implementing national treatment if necessary from a legal and implementation standpoint.

Speeding Up the Product Approval Process

The Speed to Market Working Group is responsible for identifying one-stop filing procedures and a more efficient process for State regulatory approval of insurance products marketed to consumers. State regulators recognize that under the current 50-state system, it takes far too long to introduce a new insurance product. This is not good for consumers or the insurance industry. In Dallas, this Working Group appointed two subgroups to focus its efforts on speeding up the product approval process.

The Coordinated Advertising, Rate, and Form Review Authority (CARFRA) Subgroup will develop the details for single-point product filing. CARFRA is a proposal that will assist insurance regulators in reviewing and approving rate, form, and advertising filings by creating a new centralized organization specifically tasked with that goal for participating States. It will provide insurers with a single point of contact and uniform standards for eligible products. For consumers, it will speed beneficial insurance products to market while preserving high quality regulatory review and effective consumer safeguards. At the Dallas national meeting, the Speed to Market Working Group announced that a limited launch of CARFRA will occur within the first quarter of 2001, and assigned the subgroup the responsibility for developing the operational procedures necessary to implement CARFRA.

A second subgroup, the Improvements in State-Based Systems Subgroup, which I chair, will evaluate various suggestions for improving State-based systems. It will review a list of suggestions that include, but are not limited to:

- Implementation of the System for Electronic Rate and Form Filings (SERFF) in all states. SERFF uses a point-to-point electronic communication tool where filings are sent from insurers over the Internet and routed to a State from a central server;
- Agreement on a uniform approach to filing exemptions for products sold to large commercial policyholders;
- Staffing and training of rate, form, and advertising review units to ensure quality reviews and prompt turnaround time for filings;

- Elimination of any requirements that are not published in statutes, regulations, bulletins or guidelines;
- Evaluation of prior approval requirements and movement toward market-based regulation;
- Improvements to the Market Conduct Examination process; and
- Improvements in consumer education.

The Speed to Market Working Group tasked the Improvements in State-Based Systems Subgroup with the responsibility for developing specific proposals by the December 2000 NAIC national meeting. The Working Group also heard comments from interested parties during its meeting in Dallas. Representatives from consumer interests and various sectors of the insurance industry provided input and guidance to shape the CARFRA proposal and encourage improvements to State regulatory processes. The Subgroups have planned a series of meetings during September and October, and the entire working group plans to hold another meeting in November 2000.

Facilitating the Use of E-Commerce

The NAIC E-Commerce and Regulation Working Group, which I chair, developed a resolution adopted by the NAIC earlier this year endorsing the Uniform Electronic Transactions Act and issued a self-assessment guide for use by the states to identify ten (10) potential barriers to the use of e-commerce. Within the next few weeks, the Working Group expects to adopt a Model Bulletin for use by the States to implement many of the recommendations set forth in the self-assessment guide. The NAIC has been progressive in its work to facilitate the use of e-commerce, recognizing that both consumers and insurers want the cost savings and convenience of using the internet to purchase insurance.

Ohio is a Leader in Modernizing State Insurance Regulation

I am proud to report that the State of Ohio has become a leader in implementing the policies necessary to implement GLBA and modernize state insurance regulation. In Ohio, we are committed to fostering a competitive marketplace for the benefit of consumers and the insurance

industry, and focusing our regulatory resources in priority areas that add the most value to our work of protecting Ohio consumers. Through our independent efforts and by implementing the NAIC initiatives, we are seeing real progress as we continually work to carry out these objectives.

With respect to GLBA implementation, Ohio currently has in place privacy laws that exceed the requirements of GLBA, and we plan to introduce legislation in the near future to make minor procedural changes to the law to fully comply with GLBA. We have also established good working relationships with each of our Federal agency counterparts through personal meetings involving regional heads of the respective Federal agencies. In addition, Ohio participates on the NAIC team that regularly meets with representatives of the Federal Reserve Board in Washington D.C.

Most notably, in the area of agent licensing, Ohio has led the country. Ohio was the first State that enacted reciprocal licensing for non-resident agents, and therefore, was the first State to comply with GLBA's NARAB provisions. In addition, last year, Ohio implemented a state-of-the-art internet agent licensing system that is regarded as one of the best in the country, if not the best. Using this system, an agent can submit an application on-line, pay the application fee on-line, complete the fingerprinting and background check using an electronic system, schedule a test on-line, take the test using a state-of-the art system, receive the exam results immediately after the test, walk out with a license if successful, and obtain a company appointment on the same day using our internet appointment process, all of which takes less than 7 days. Because of this work, Ohio was selected to be one of the four pilot states for the National Insurance Producer Registry, which was launched earlier this month. As stated previously, NIPR will allow one-stop licensing for non-resident agents in all 50 States.

With regard to insurance regulatory modernization initiatives, Ohio is also a leader. Just yesterday, I signed two regulatory bulletins that will allow 81% of all property and casualty insurance products to be submitted on "file and use" basis. I plan to seek legislation that will move our product filing system to a file and use system for all appropriate products and exempt certain products and rates from the filing requirement altogether where appropriate. For

example, just yesterday, I signed a bulletin that exempted from the filing requirements all Special Filings and Excess Rate Consent Filings. To support these initiatives, Ohio was among the first – and was the fastest – to introduce the NAIC-sponsored System for Electronic Rate and Form Filing (SERFF). SERFF will be a vital tool for implementation of CARFRA and improving the filing and approval process for products not selected for the CARFRA process. Ohio has already received 165 property and casualty filings since March 2000, and we believe the new web-based version of SERFF, scheduled for release in October 2000, will open the door to widespread use among the industry and all of the States.

As noted earlier in my testimony, as Director of Ohio Department of Insurance, I chair the NAIC's E-Commerce and Regulation Working Group, the goal of which is to facilitate the use of e-commerce, and the Improvements to State-Based Systems Working Group, the goal of which is to improve the State-based insurance product approval process.

We look forward to the continued positive impact these initiatives will have on our work to protect consumers through an efficient and effective regulatory system.

Congress Can Help Improve State Regulation

Improvements in several Federal laws affecting State insurance regulation would help give us all the tools we need to meet the challenges of the modern marketplace. During Congressional consideration of GLBA, the NAIC suggested several amendments to Federal laws that would be useful.

The primary benefit of making the following changes to Federal laws is to achieve uniform regulatory procedures and national enforcement quickly by using the existing system of State regulation. The NAIC proposes that Congress –

- Provide State insurance regulators with access to the national criminal information database (NCIC) through the NAIC or its affiliates for regulatory purposes and for

checking criminal histories as required by the Federal Insurance Fraud Prevention Act. (18 USC 1033)

- Grant Federal immunity from liability for NAIC and NIPR database activities related to creating a national licensing and enforcement system.
- Protect the confidentiality of regulatory communications among NAIC, State regulators, and Federal agencies.

NAIC and its members will be pleased to provide additional information and assist Congress in adopting Federal legislation to achieve these goals.

Conclusion – State Regulators Are Meeting the GLBA and Modernization Challenge

Working together through the NAIC, Ohio and other State insurance regulators are well on the way to implementing the provisions of GLBA as intended by Congress. More importantly, we have shown real progress in our efforts to do far more than Congress or industry representatives have asked us to do regarding uniformity, efficiency, and modernization. We look forward to working with Congress, our Governors and legislatures, and all other interested parties as we continue to develop and implement the GLBA required regulations and legislation, and our State insurance regulation modernization initiatives.