STATEMENT

OF

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ON BEHALF OF THE

AMERICAN BANKERS INSURANCE ASSOCIATION

TO THE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

OF THE

UNITED STATES SENATE

EXAMINATION AND OVERSIGHT OF THE CONDITION AND REGULATION OF THE INSURANCE INDUSTRY

July 11, 2006

Chairman Shelby, Ranking Member Sarbanes and Members of the Committee, my name is Alan Liebowitz, and I am President of Old Mutual (Bermuda) Ltd., an insurance company affiliated with the Old Mutual Financial Network. Old Mutual is a global diversified financial services network that extends from Europe to Asia, Africa and North America. In the United States, the Old Mutual Financial Network provides retirement savings and financial protection products in all 50 States through Fidelity & Guaranty Life, Americom Life & Annuity, and Fidelity & Guaranty Life of New York. Our life insurance companies have combined assets of over $12 billion and serve nearly 650,000 policyholders.

I am here today on behalf of the American Bankers Insurance Association (ABIA), the insurance affiliate of the American Bankers Association (ABA). ABIA's members are banking institutions that are engaged in the business of insurance and insurance companies and administrators that provide insurance products or services to banks. Together with our colleagues at the American Council of Life Insurers, the American Insurance Association, the Council of Insurance Agents and Brokers and many other trade associations, ABIA and ABA participate in the Optional Federal Charter Coalition.

I began my professional career as a lawyer in a firm specializing in insurance regulatory matters. I dealt primarily with insurance departments on company formation, licensing and corporate governance. From there, I became general counsel to a New York domiciled life insurer where I dealt with all legal issues including licensure in 17 states, policy drafting, filing and advertising compliance.

I joined the largest U.S. bank holding company in 1985 and for 15 years represented it on insurance related issues including the Bank Holding Company Act and 50 state insurance laws. It was during this period that the contrast between bank and insurance regulatory schemes became starkly evident. It became abundantly clear to me that consumers were not benefiting from the insurance regulatory system and, in fact, were being denied access to more affordable and creative products by virtue of the constraints placed on insurers in the name of consumer protection. I see very little today indicating that this deficiency has been addressed. What changes have occurred have taken place at the margins of reform, have been incomplete and have only been in response to congressional action.

Since 2000 I have been president of Old Mutual (Bermuda) Ltd., a Bermuda domiciled insurer that focuses on delivering primarily U.S. capital market based products around the world through financial institution distribution. This experience has made me familiar with the insurance laws of many countries, including the United Kingdom, Hong Kong, the Middle East, Israel, Mexico and various Latin American countries.

The differences between foreign insurance regulatory structures and our own are as stark as the differences between our banking and insurance systems. In these countries, unlike the United States, insurance regulation is uniform. As a result, consumers and insurers are not subject to policy or pricing differences simply because of their location. Meaningful reform to the insurance regulatory system must be instituted in the United States to keep our home markets healthy and to address the growing competitive disparity between our domestic market and the markets of other nations. To me, the problem is simple: the states seem capable of only debating reform; instituting reform occurs only when Congress acts.

No where is this more true than in the three regulatory areas most at issue for bankers selling insurance products: producer or agent licensing, product availability and price controls. These regulatory functions are executed differently in every one of the 56 US jurisdictions. Regulating insurance in this fashion is inefficient and provides little benefit to the consumer. For example, after centuries of experience watching free markets efficiently determine prices for other products to the overwhelming benefit of consumers, we in the United States continue to allow the states to set the price of insurance products. In addition, there is no uniform product regulation whatsoever among all 50 states. And, perhaps most importantly, it took an act of Congress before 40 states - and to date only 40 states - instituted a reciprocal, but not uniform, agent licensing system.

Problems with the Current Insurance Regulatory System

Producer Licensing

Creating a single standard for licensing agents should have been easy. It should have been work the states completed more than a century ago but little was done about instituting uniform agent licensing until 1999 when passage of the Gramm-Leach-Bliley Act (GLBA) forced the states to adopt act. In 2000, the National Association of Insurance Commissioners (NAIC) said its goal was the "*implementation of a uniform, electronic licensing system for individuals and business entities that sell, solicit or negotiate insurance.*" Six years later, that goal has yet to be realized.

Currently, different States impose different qualification and testing standards and different continuing education requirements on producers. Licenses recognized in one State are not necessarily recognized in another State. Worse, agents associated with banks are sometimes subject to sales limitations not applicable to agents who are unassociated with banks. For banks that operate agent networks in multiple States, these differences impose compliance costs and other financial burdens that are significant and, ultimately, borne by consumers.

In 1999, as part of GLBA, Congress adopted a requirement designed to promote the adoption of uniform agent licensing rules by the states. The so-called NARAB provision of GLBA required the establishment of an organization to develop uniform licensing rules and regulations, but only if a majority of the States did not adopt either uniform or reciprocal licensing laws and regulations within three years of the date of enactment of GLBA. To facilitate compliance with GLBA, the NAIC developed a <u>reciprocal</u> licensing Model Act, which has currently been adopted by about 40 States. Because the States could avoid NARAB – and the uniformity mandate it represented - if only a majority of States enacted the Model, that action by a majority of States has allowed some States, including some of the largest States like California, to avoid the issue of licensing reform entirely.

And, the more important goal of achieving licensing <u>uniformity</u> has been put off indefinitely. GLBA allowed the goal of uniform agent licensing laws to remain unrealized so long as a majority of States passed reciprocal licensing laws. <u>Unfortunately, reciprocity is not uniformity</u>. Instead, it is the recognition and acceptance of differences among States. Seven years after passage of GLBA, significant differences in State licensing laws remain.

To solve this problem, I recommend adoption of a uniform agent licensing standard, preferably through the creation of an Optional Federal Charter. The proposed National Insurance Act, S. 2509, introduced by Senator John Sununu (R-NH) and Senator Tim Johnson

(D-SD), creates a uniform agent licensing standard by allowing agents to apply for a National Producer License. This national license would allow an agent to sell insurance products anywhere in the United States and would not compel the states to change their laws at all. By definition, the National Insurance Act creates a regulatory framework for insurance much like the dual banking system with which we are all familiar. While the licensing provisions establish a national producer's license, they do not require state-licensed agents to obtain that license in order to sell the products of federally chartered insurers.

The result is a competitively neutral agent licensing regime. Agents who desire only a state license will be able to sell exactly the same array of products in their state as a federally licensed agent operating in the same state. Alternatively, an agent who needs to sell products in multiple states will not have to obtain the individual state licenses offered by every state but may instead obtain the federal license offered under this Act. By offering the federal license as an option to the existing system of state licenses, the Act preserves the authority of states to regulate agents licensed in their states but also allows those desirous of the efficiency a single federal license offers the ability to obtain one.

Rate Regulation

Three basic components are necessary to provide for the insurance needs of consumers: an agent has to be licensed to sell insurance products, there have to be products to sell and those products must be at prices consumers can afford. Price controls have long been thought to satisfy this latter requirement but, in fact, they work against consumers' interests in the overwhelming majority of cases.

In most States, an insurance product can only be sold after the State insurance regulator approves the price of an insurance product. Some States regulate the price of an insurance policy; some States regulate the loss ratio a given product line must maintain. Generally, the effect of price controls has been higher prices and fewer choices. When prices are set artificially high, consumers are denied access to lower costs even if there is a willing seller. When price controls are set artificially low, the number of willing sellers is reduced resulting in greatly diminished consumer choice.

Price controls are only appropriate, arguably, when associated with a utility or a monopoly. In such situations, a single company could set and hold prices at unreasonable levels. The insurance industry, however, is a competitive industry. There are thousands of insurers operating in the United States, and the only significant barrier to entry for new companies is the cost of compliance with the kaleidoscope of state insurance regulations and the inability to adjust prices based on market forces. In such a competitive market, competition among firms will protect consumers from unfair pricing schemes much more efficiently than the government. More importantly, allowing markets to set prices efficiently controls risk by making riskier choices more expensive.

The consumer benefits associated with competitive rates are more than just speculative. Several States already have moved away from rate regulation and, in those States, there is evidence that rates have fallen on certain products. A study by Scott Harrington for the AEI-Brookings Joint Center for Regulatory Studies entitled "Insurance Deregulation and the Public Interest" found that auto insurance is less costly and more available in 14 States that do not require prior approval of rates than in 27 other States that do require prior approval.

I have arrived at the same conclusion as Mr. Harrington. As a nation, we allow markets to set the price of housing, food and clothing, necessities more instrumental to the survival of most of us than insurance products. There is no basis for allowing the government to continue setting prices for insurance products when it's clear we are only saving consumers from lower prices and more choices.

Product Approval

Similar to price controls, most States' insurance departments won't approve an insurance policy for sale unless subject to prior review by the insurance regulator. ABIA's members have found that the impediments created by most States' prior approval requirements have had the undesirable effect of depriving consumers of innovative insurance products and retarded the ability of insurers to develop these products in a timely fashion.

Under the current State system of insurance regulation, it can take months, and sometimes years, for a company to receive permission from State insurance regulators to introduce a new product in every State. Such delays are an inevitable result of a system in which every State has an opportunity to review and approve insurance products and where the standards of review are different in every State. If the insurance industry cannot gain some relief from the States' prior approval regime, life insurers will continue to lose market share to other non-insurance investment products and property and casualty insurers will reduce or eliminate their efforts to develop innovative products that offer more comprehensive benefits at lower costs.

To alleviate this problem I recommend adoption of an insurance regulatory system with many of the features of the current banking system. Instead of prior review of insurance forms, a system like the one proposed in S. 2509 should be adopted. Under such a system, the National Insurance Commissioner would establish regulations for insurance products, require forms to be filed with the Commissioner, examine insurers for compliance with these regulations and impose strong penalties for non-compliance. Senators Sununu and Johnson are not proposing de-regulation of insurance products but, instead, a more permissive system patterned after banking regulation and designed to promote, rather than slifle, innovation.

Consumer Benefits of Creating an Optional Federal Charter

ABIA's member companies design systems and products to suit the needs and demands of consumers. Accordingly, we recognize that any insurance modernization proposal must be responsive to those needs and demands. The proposed National Insurance Act introduced by Senator Sununu and Senator Johnson will advantage consumers by allowing them access to a wider array of products at more competitive prices. The proposed legislation will also ensure that companies are more financially sound, and that the United States insurance industry is better represented abroad. Foreign financial regulators tend to agree: Commenting in the *Financial Times* last week, Sir Howard Davies, Director of the London School of Economics and a former chair of Britain's Financial Services Authority, observed that,

> *"There is no federal regulator or federal charter available to US companies. As a result, there is a lack of leadership in insurance regulation nationally and internationally. This is unfortunate when insurers are engaged in far more complex financial transactions than they used to be. Many US insurers would welcome the opportunity to seek federal oversight: the Treasury could make it possible for them to do so. A positive side-benefit would be to strengthen US influence in the International Association of Insurance Supervisors and make it more effective in dealing with problems of unregulated insurers and reinsurers in offshore centres."*

I agree with Sir Howard. Establishing an Optional Federal Charter will assist the United States in remaining globally competitive in two important ways. Firstly, the current regulatory system greatly impedes our ability to negotiate in the international regulatory arena. Whereas most countries are represented by a single federal regulator, like in Great Britain, the United States is represented by a variety of state insurance regulators who, by definition, do not and cannot speak for the United States.

Secondly, the difficulty of entering the U.S. market under the current state regulatory system dissuades foreign capital from investing in the U.S. market, restricting overall insurance capacity, and reducing the number of insurance products available to U.S. consumers. It is simply the case that there are relatively few foreign companies willing to expend the time and resources necessary to navigate our confusing state regulatory system. By that measure, it is also the case that there are many American companies that do not have the resources to enter every state's market. In that regard, foreign insurers and small domestic insurers share the same problem: the benefit of entering every state's market does not equal its cost.

But, improving American competitiveness in the global insurance arena is only one welcome benefit of the proposed National Insurance Act. The real merit is in the myriad ways consumers are advantaged and I will detail them for you now.

Consumer Access to Sound Insurance Products

An insurance policy is a promise to pay benefits after a triggering event. An often overlooked consumer benefit in S. 2509 is the imposition of rigorous financial solvency standards for federally chartered insurers. These standards include risk-based capital requirements ensuring that National insurers are adequately capitalized; Investment standards ensuring that National insurers invest their assets prudently; and, dividend restrictions, which prevent insolvent National insurers from paying dividends. Such standards should give consumers confidence that a Federally chartered insurer will be able to pay claims on its policies.

The proposed National Insurance Act ensures Federal solvency standards are met by requiring regular examinations and setting forth enforcement measures for non-compliance. These examination and supervisory powers are designed to ensure that Federally chartered insurers are safe and sound. Examination and enforcement standards contained in S. 2509 include: the authority to require Federally chartered insurers to file regular reports on their operations and financial condition; the authority to regularly examine Federally chartered insurers, and to the extent appropriate, their affiliates; and the authority to initiate an enforcement action against Federally chartered insurers that fail to comply with applicable standards. Enforcement penalties are patterned after those available to Federal banking regulators, which include the power to remove officers and directors and to impose civil money penalties of up to $1 million a day.

These standards are significantly more stringent than what exists at the state level today.

More Rigorous Market Conduct Standards.

The proposed National Insurance Act also protects consumers through Federal market conduct standards. Currently, market conduct exams are performed inconsistently by each state's insurance regulator. Some states are rigorous; some states are not. Some states impose market conduct examinations on insurers and insurance brokers by requiring them to hire a consultant selected by the states. The proposed National Insurance Act would protect consumers by preventing unfair methods of competition and unfair and deceptive acts and practices in the advertising, sale, issuance, distribution and administration of insurance policies through a single, uniform examination standard, a routine examination cycle and strict penalties for non-compliance.

Critics of optional federal chartering often claim that a Federal insurance regulator would not be able to adequately police sales and claims practices by National insurers or producers. The Federal regulation of the banking industry shows that Federal agencies can effectively enforce consumer protection standards.

Today, thousands of banks are offering a variety of products to consumers through hundreds of thousands of branches, ATMs, loan production offices and other outlets throughout the United States. These banks are subject to Federal consumer protection statutes such as the Truth-in-Lending Act, the Truth-in-Savings Act, the Fair Credit Reporting Act, the Equal Credit Opportunity Act and many others. The Federal banking agencies, which are responsible for enforcing compliance with these various consumer protection laws, have been able to fully and effectively enforce compliance with the laws. They have done so through a combination of regular examinations backed up by the threat of enforcement actions. Federal market conduct standards for insurers backed by examinations and the threat of enforcement should work equally well for consumers of insurance.

Consumer Benefits of Uniformity

Nationwide uniformity of policies and sales practices that would be created by S. 2509 reduces consumer confusion, especially for those consumers who move from State to State for professional or personal reasons. Under the proposed National Insurance Act, the same life insurance policy could be offered in every State. Companies could use the same policy form, same disclosure statements, and same administrative procedures throughout the United States. A consumer who moved from New Jersey to New York, and then to Connecticut would have the same purchasing experience in each state if the product being offered was issued by a National insurer.

Uniform regulation also facilitates delivery of insurance products over the Internet. As we all know, the Internet can reach consumers, regardless of where they are located. To date, however, the use of the Internet to deliver insurance products has been complicated by variations in State insurance sales laws. A single Federal sales practice standard applied nationwide would eliminate such complications. This would expand consumer access to insurance products through the Internet. The proposed National Insurance Act would make expanded Internet sales a reality.

Conclusion

ABIA has concluded that the current insurance regulatory system is badly in need of reform and, judging by the organizations represented here today, we are not alone in that conclusion. Virtually all industry participants and even insurance regulators have spent years detailing the failings of the State system. The question, therefore, is not *if* the system needs reform but *how* to reform it. Some organizations would prefer to let the states continue the unacceptably slow process of reforming themselves. Others believe Congress should impose federal insurance standards on the states. We believe Senator Sununu and Senator Johnson have defined the appropriate solution; namely, an Optional Federal Charter for insurers and insurance producers. The "Optional Federal Charter" solution addresses the shortcomings of the existing State insurance regulatory system by creating a national regulatory framework, yet preserves the State system for those who prefer it.

The proposed National Insurance Act is the path forward and we urge the Committee to consider it at its next opportunity.