COMMITTEE: **STANDING COMMITTEE ON COMMUNICATIONS, FINANCIAL SERVICES & INTERSTATE COMMERCE**

TITLE: **INSURANCE REGULATORY MODERNIZATION**

TYPE: **DRAFT POLICY STATEMENT**

The National Conference of State Legislatures (NCSL) is committed to state regulation of the business of insurance. Insurance serves as the cornerstone of the economy. It provides economic security for individuals and their families and allows businesses to manage the risks that are inherent in economic activity. Whereas banking and securities are about access to capital and risk-taking, insurance is a guarantee. It is a legal promise—steeped in state tort and contract law—to provide benefits if and when they are due, often years into the future.

For more than 150 years, the states have proven that they can successfully and effectively protect consumers and ensure that promises made by insurers are kept. As a different kind of financial service, insurance requires a different kind of regulation that the states are best suited to provide. State regulation ensures that rates are fair, adequate and not excessive; that policy language is clear and includes what it should; that insurers are financially sound; that claims are paid; that consumers are informed, and that their complaints are investigated and resolved.

State regulation is accessible, accountable and responsive, and operates with greater efficiency than would a vast new federal bureaucracy. Decentralized authority promotes regulatory innovation and safeguards against the imposition of regulatory controls with potential adverse consequences that would be national in scope. Furthermore, state legislatures are uniquely positioned to set policies that accurately reflect local values and concerns, and the nation as a whole benefits from regulation tailored to serve diverse economic, social and cultural needs as well as varying geographic and environmental conditions.

Insurance Regulation for the Modern Economy

Although strongly committed to the preservation of state insurance regulation, NCSL acknowledges the responsibility of states to adjust state systems to meet the needs of the modern economy. The Gramm-Leach-Bliley Financial Modernization Act of 1999 (GLBA) tore down Depression-era barriers and created a comprehensive framework to permit affiliations among banks, insurance companies and securities firms. GLBA also compelled state actions in the areas of producer licensing and insurance information privacy while implicitly calling on states to modernize insurance regulation.

States accepted this challenge with remarkable vigor. State legislatures and commissioners quickly met the specific mandates of GLBA. They continued to develop a shared vision of insurance regulatory reform to meet the needs of the modern marketplace while preserving the advantages of the state system. NCSL recognized the importance of state legislatures taking a proactive role, and therefore established a special task force to streamline and simplify insurance regulation. NCSL worked with insurance commissioners to draft and endorse the Interstate Insurance Product Regulation Compact, which creates a national state-based system to quickly make regulatory decisions on life insurance products according to uniform national standards.

The National Conference of State legislatures has endorsed state participation in the Interstate Insurance Product Regulation Commission and by January 1, 2009, at least 35 states will be participatory members.

NCSL also adopted an insurance regulation statement of principles, which encourages states to consider more competitive systems of product regulation for property and casualty insurance to promote the more efficient introduction of new products into the marketplace while preserving their authority to take action in a noncompetitive market and against rates that are inadequate or unfairly discriminatory. The statement continues to encourage state legislatures to:

- Direct insurance commissioners to simplify and streamline regulatory standards and requirements and eliminate inefficient and redundant regulation;

- Allocate greater insurance department resources to market regulation, anti-fraud and financial solvency efforts;
- Support regulatory efforts to improve market regulation; create more efficient, effective and uniform market conduct examinations; promote the use of technology; and better coordinate with other states; and
- Exercise oversight and investigatory functions to evaluate modernization efforts at the regulatory level and encourage industry participation in improvements to state-based systems.

State-Federal Partnership

Working individually and at the national level, states since the passage of GLBA have worked to modernize insurance regulation. However, state legislatures recognize a legitimate federal role in overseeing and promoting well-functioning insurance markets. Therefore, NCSL is willing to work with Congress to establish a shared state-federal framework to achieve insurance regulatory modernization that focuses on areas where policymakers have reached consensus and that preserve state flexibility and authority to meet the goals of modernization. However, NCSL will oppose any provision of federal legislation that relies on wholesale preemption of state authority; that would compel state compliance with federal standards or those of any non-governmental third party; or that conditions, restricts or redirects state insurance revenues, including insurance premium taxes, fees and fines, either directly or as a condition of a state's refusal to submit to federal standards or federal efforts to commandeer a state executive branch official to participate in a federal regulatory program.

In recent years, states have enacted a wide range of reforms in critical areas to streamline, simplify and coordinate state systems and to establish uniform regulations and processes, where appropriate. NCSL believes that state efforts to enact significant reforms in critical areas represent tremendous progress and will continue to support further efforts as states move forward to achieve widespread reform in all areas in the years ahead. Some in Congress have criticized states for not moving more rapidly; however, NCSL believes that it is appropriate that modernization efforts be based on deliberate consideration. Reforms must balance legitimate industry needs for efficient, appropriate and transparent regulation with the goals of preserving and enhancing important consumer protections and financial safeguards, which are the hallmarks of the state system. State lawmakers and insurance commissioners must carefully measure these shared priorities as they move forward and should resist efforts from Congress and interested parties to prematurely embrace wholesale reforms in a blind race for uniformity.

Moreover, some in Congress and industry support federal legislation to establish a single federal regulator of insurance or allow for dual federal and state insurance regulation. If enacted by Congress, such proposals would eliminate or diminish state insurance regulation irreparably, bifurcate insurance regulation between the states and the federal government, undermine the state system of consumer protection and financial surveillance, threaten a host of other unintended consequences, and inevitably cause a loss of jobs, taxes, fees and other critical state revenues and resources. Therefore, NCSL opposes any provision of federal legislation that preempts state authority through the creation of a federal insurance official, commission or entity with the authority to regulate insurance, to implement federal standards, to enforce state compliance with federal standards, or to initiate or participate in judicial proceedings to resolve differences between federal standards and state law.

The National Conference of State Legislatures calls upon Congress to review what impact the Gramm-Leach-Bliley Financial Modernization Act had had on the current mortgage crisis that has continued to wreak havoc on the American economy. In light of the magnitude of the impact of the mortgage crisis on numerous financial services providers, Congress needs to address the impact of national regulation before it carelessly erodes the strength of a state based insurance regulatory system.

Insurance Company Solvency

The safety and soundness of insurance companies operating in the United States are the prime objectives of state insurance regulation. To ensure that these objectives are met, an effective financial surveillance and regulation system is vital. State legislatures have endeavored to strengthen state insurance departments and to create standards for financial regulation that have improved the solvency of insurance companies.

Although successful and effective, state solvency regulation standards should be reviewed and modified on an ongoing basis in order to meet the changes of a constantly evolving financial services marketplace. In doing so, states are protecting insurance company policyholders and investors. The public depends on solvent insurance companies to provide retirement income, income protection in case of death or disability, health care coverage, protection from catastrophic loss, and safe investment opportunities.

Swift and effective action by state legislatures to reform state solvency regulation proves that states are more capable of adjusting to changes in the marketplace than Congress or federal regulatory agencies. NCSL therefore will oppose any proposal to establish federal standards for state solvency regulation that cedes any authority to federal agencies to regulate financial institutions involved in the business of insurance and congressional ratification of trade agreements that would preempt state regulation of insurance for solvency purposes. Although NCSL continues to support the NAIC Financial Regulation Standards and Accreditation Program, NCSL acknowledges that state legislatures and governors have the responsibility to enact policy, which state regulators enforce. NCSL also recognizes that interstate compact proposals have the potential of addressing binding uniformity and effectiveness in specific areas of regulation.

NCSL also objects to actions taken or contemplated by the Internal Revenue Service or other federal agencies to assert priority claims to the assets of failed insurers. The states should first be allowed to distribute an insolvent company's assets to pensioners, family businesses, other policyholders and others protected by the McCarran-Ferguson Act delegation for the business of insurance to the states.

In the same vein, NCSL is concerned by federal bankruptcy rulings under the federal bankruptcy code that would allow alien insurers and reinsurers to move certain trust fund assets to bankruptcy proceedings in their domicile country. The trust funds established by alien insurers and reinsurers are to serve as collateral for insurance and reinsurance underwriting in the United States and allow such alien insurers and reinsurers to be exempt from state solvency regulation. Federal bankruptcy courts in ruling in favor of alien insurers and reinsurers have placed these collateral trust funds out of the reach of state insurance departments, which are solely responsible for solvency protection. NCSL urges Congress to rectify this situation by amending federal law to eliminate or limit this exemption for alien insurers and reinsurers under the bankruptcy code.