

» Policyholder Protection in an Age of “Regulatory Fury:”

The Double-Barreled Expansion of Insurance Oversight and What it Means for the Guaranty Fund System

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NCIGF 2013 Fall Workshop
Amelia Island, Florida

» Every Element of Insurance Regulation is on the Table

- The tectonic plates are shifting
- Why?
- Post-crisis, globalization and increased risk

» Can These Risks Be Managed?

- Dysfunction in Washington is Unquestionably a Systemic Risk
 - Affects every industry
 - Institutional investors concerned when dysfunction threatens default
- Persistently Low Interest Rates
- Rising Catastrophe Loss Trends/Climate Change
- Terrorism (TRIA Reauthorization Debate)
- Cyber Risk
- Proposed New FASB Accounting Rules for Insurance
- Insurer Board of Director Governance Issues

» Fundamental question to be decided over the next several years

- What will insurance look like?
- Risk-sharing or Income transfer?
- Preview: Affordable Care Act

» Impact on Guaranty Funds

- “The changes underway will alter the basis for much of your work in ways that are not yet clear.”

William P. White, Commissioner D.C
Department of Banking and Insurance
October 26, 2013

» First, Something Upbeat: The GAO Report

- With Few Exceptions, GAO Found That the Effects of the Financial Crisis on Insurers & Policyholders was Limited
- State & Federal Regulators & the NAIC Helped Limit the Effects of the Crisis
- Continued Regulatory Efforts Since the Crisis Have Focused on Insurers' Risks, Capital Adequacy & Oversight of Noninsurance Entities in Group Holding Company Structures.
- *NCIGF was interviewed for this report in our role as trusted expert*

» The First Barrel

Dodd-Frank Implementation

» Dodd-Frank Enacted July 21, 2010

- Title II resolution mechanism for liquidating systemically important financial institutions
- FDIC gets most of these, but all insolvent insurers remain subject to state receivership and GF processes

» New FDIC Powers are Relevant to the GF System

- The new Office of Complex Financial Institutions: staffed up and ready to go!
- Complex process: FDIC could provide liquidity to insurer owned by a troubled SIFI, to buy time for a coordinated resolution or to side-step the state liquidation process altogether

» Federal Insurance Office

- Annual Report issued
NCIGF interviewed; our charts are in the report
- The Elusive Modernization Report: -
---Due January 2012, but **nowhere** to be seen

» No FIO Report, so no problem, right?
Not exactly

- FSOC Determinations:
AIG & Prudential deemed Systemically Important Non-Banks
- Enhanced supervision by the Federal Reserve.
- Welcome to the World of Federal Insurance Regulation!

» The Second Barrel

International Regulation of Financial Services

» Why is this happening?

- Overall premium Growth in Emerging Markets was **Four Times** That of Advanced Economies in 2012:

Advanced: +1.7%

Emerging: +6.8%

World: +2.4%

» International Association of Insurance Supervisors

- International standard-setting body for the prudential supervision of the insurance industry
- Began developing a Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) in July 2010.

» ComFrame has three main objectives

- Develop methods of operating group-wide supervision of IAIGs
- Establish a comprehensive framework for supervisors to address group-wide activities and risks, and
- Fostering global convergence.

» The NAIC's International Involvement

- Increasingly focused on strengthening the supervision of insurers that operate in multiple countries, or IAIGs
- A key focus for the Solvency Modernization Initiative (SMI) project has been enhancing group supervision.
- The NAIC's International Insurance Relations (G) Committee supports the work of the IAIS by participating in Executive, Technical and other relevant Committee meetings, and by drafting and commenting on papers to represent the views of U.S. insurance regulators.

» Safety Nets Attracting Interest

- 2010 European Union began process to ensure that all member states have a PH protection scheme that meets minimum requirements.
- Not out yet, but expected yet this year or early 2014
- Resolution procedures are being discussed as part of ComFrame but standards await further work on solvency measures

» IAIS Paper on Policyholder Protection Mechanisms

- Drafts have circulated for over a year.
- We've commented on at least 8 drafts
- NCIGF appeared before IAIS committee Spring 2012
- Published October 2, 2013

» IAIS PPS Conclusions

- Design should be based on nature of the insurance industry as well as cultural and legal framework
- PPS as the last resort; effective regulation and liquidation schemes should come first
- Close cooperation, early intervention are critical to minimizing disruption and protecting policyholders

» The Rise of the Financial Stability Board

- Established in 2009 by the G-20 nations
- Develops and promotes implementation of regulatory and supervisory policies aimed at financial stability
- US Members are the Federal Reserve, SEC and Treasury
- Even though there's no insurance expertise on FSB, its taking a more active role in the insurance sector s evidenced by....

» FSB: Staying Busy

- Peer Review of U.S. System of Insurance Supervision
- Designation of G-SIIs 7/18/13: AIG, Prudential, Metropolitan, Allianz, Aviva, Axa, Generali, Ping and Prudential P/C

» FSB: Key Attributes of Effective Resolution Regimes for Financial Institutions

- The Key Attributes require powers very similar to what the U.S. now has between the state guaranty funds and Title II authority granted the FDIC under DFA
- NCIGF-NOLHGA Joint Comments Made this point

» International Association Insurance Supervisors 20th Annual Meeting

- HEADLINE: Capital Standards for GSIs in 2014 and IAIGs in 2016
- Required by FSB
- Proposition that adequate group capitalization does not=adequate insurance capitalization
- Federal Reserve Applies for Membership in IAIS.

» Significance of Capital Standards

- Will apply to insurance companies of ALL sizes, possibly as early as 2019
- Higher Loss Absorption
- Capital is King!

» Concerns About Insurance Capital Standards

- No relation between capital standards and the actual operation of insurance business
- No consideration of how risk is measured and how insurance products are priced in response

» What are the Capital Standards Trying to Accomplish?

- “One of the questions I have is whether we are trying to prevent company failures or control the effects?”

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» The Road Forward (Part 1)

- Do what we do and continue to find ways to do it better
- GF are the continuity in US Liquidations
- Identify and fill gaps
- Use regulatory change to make improvements that we want to make anyway, i.e. D Record, Data Management, Imaging

» The Road Forward (Part 2)

- Pro-active assertion of the U.S. Safety Net Model;
- Engagement is critical, essential and unavoidable
- Perceived weaknesses:
 - *Capacity * Consistency * Decentralization

» The Road Forward (Part 3)

- Keep Regulators and Industry Informed of What We Are Doing
- Use our status as “trusted experts”
- Feel the same pain as everyone else
- Accept, understand and answer the questions being asked

» Conclusion

- Disappointed that US regulators don't "get" GF System
- Lots of politics involved
- Dodd-Frank still the law as are the state statutes that create GFs— still change is likely.
- Recent developments underscore importance of engagement with key policymakers
- Don't know how many minds we can change but we have to do everything we can to strengthen our system and our message
- We didn't pick this fight, but it's one I'm in to win!