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NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Statement

of the

National Association of Mutual Insurance Companies

to the

United States Senate

Committee on Banking, Housing and Urban Affairs

Hearing on

The Role of the Financial Stability Board in the U.S.

Regulatory Framework

June 8, 2015

The National Association of Mutual Insurance Companies (NAMIC) is pleased to provide comments to the Senate Committee on Banking, Housing and Urban Affairs on the role of the Financial Stability Board in the U.S. regulatory framework, in particular the framework for property/casualty insurance companies.

NAMIC is the largest property/casualty insurance trade association in the U.S.A., serving regional and local mutual insurance companies on main streets across America as well as many of the country's largest national insurers. NAMIC's 1,300 member companies serve more than 135 million auto, home and business policyholders, and write more than $196 billion in annual premiums.

Introduction

Over the last several years, the Financial Stability Board (FSB) has become an increasingly important and influential regulatory organization for the global financial services sector. Re-established in the wake of the financial crisis, the FSB's core mission is to promote regulatory standards that ensure the stability and soundness of the world's financial system. Pre-crisis, the Financial Stability Forum had a role of monitoring, coordinating, and communicating between regulatory jurisdictions. However, the mandates provided in the FSB's charter go well beyond generally-expressed objectives and require that the FSB assume a direct role in monitoring how various countries implement global rules at home.

NAMIC has significant concerns with many of the activities at the FSB, including the designation process of Global Systemically Important Insurers and its influence on the Financial Stability Oversight Council's designation of Systemically Important Financial Institutions here in the U.S. However, for purposes of these comments, we would like to focus on the FSB's review and guidance of the policy development work of international standard setting bodies, specifically the International Association of Insurance Supervisors (IAIS).

NAMIC believes the current U.S. state-based insurance regulatory system is robust and well-positioned to meet the needs of the nation's insurance marketplace. However, NAMIC has serious concerns about recent international standard-setting efforts – being pushed by the FSB – that have moved beyond development of principle-based standards. Instead, these efforts have increasingly involved initiatives to prescribe particular accounting practices and capital standards, potentially undermining our state-based insurance regulatory system. All NAMIC member companies – those that are domestic-only and those that are internationally active – will feel the impact of the international standards being imported to the U.S. Indeed, the movement toward more formulaic, prescriptive standards seems to be accelerating.

Financial Stability Board Driving Action on New Insurance Capital Requirements

In 2012, the G-20 and FSB were focused on banks as well as identifying Global Systemically Important Financial Institutions (and Global Systemically Important Insurers [G-SIIs]) and developing a new regulatory framework for them. The FSB enlisted the help of the IAIS in identifying G-SIIs for designation and with the crafting of new regulations for them. Then, without warning or clear reasons, in the summer of 2013 the FSB met with IAIS leadership and informed them that, in addition to G-SIIs, other large internationally active insurance groups (IAIGs) should also adhere to a global consolidated capital requirement that was similar to the Basel II and III requirements for banks. The IAIS was ordered to design, field test and adopt such global capital requirements first for G-SIIs by the end of 2014 and then for the IAIGs by 2016. The pace of this edict was unreasonable and unworkable, but the IAIS leadership indicated they had no choice but to comply.

Since the FSB's mandate, the IAIS Executive Committee has made numerous decisions regarding the structure and design of the international capital standard (ICS) for the IAIGs without actually stating the problem the FSB was trying to solve, and without explaining why the decisions were made. The most troublesome of these decisions include: a) the insistence on a highly detailed, prescriptive formula for the ICS that would be applied to all countries; b) the requirement that all countries use the same valuation/balance sheet without regard to the costs and implications; and c) the insistence that the capital resources that companies use to meet the obligation be identical even when the capital instruments available to companies vary across countries.

Since 2013, NAMIC has submitted comments and testified at the IAIS on numerous occasions to encourage IAIS members to listen to a different perspective. We have met with state regulators and federal officials to urge them to make these arguments as well. While there has been some recent success resulting in a delay in the "ultimate" standard, the IAIS is holding firm on many of the decisions it made in 2013.

Despite the goals of the IAIS to achieve a comparable ICS for all IAIGs around the globe, the application of the same capital standard to unique companies that come from very different regulatory environments with very different economic and political objectives will not produce comparable indicators of capital adequacy or solvency. Every country has a unique regulatory system with unique features that influence the solvency of the companies doing business in that regulatory environment. Similarly, every insurance group has unique characteristics that cannot be fully captured in a single one-size-fits-all formula. In their zeal to achieve comparability, the FSB – through the IAIS – will succeed only in generating unnecessary costs to governments and insurers.

The costs to the U.S. will not be insignificant. In fact, our country may be required to make major changes to its supervisory, corporate law, and accounting systems to accommodate the new group capital requirements. Because the new standards being contemplated are largely derived from existing European standards, U.S. insurers will be placed at a competitive disadvantage relative to their European counterparts. NAMIC has asserted that a successful global effort would not create unnecessary competitive asymmetries between companies domiciled in different, but equally well-supervised, jurisdictions. Instead, what is needed is a flexible and dynamic capital assessment that would recognize and improve understanding of diverse, successful approaches to solvency regulation. Such an approach would be principle-based and outcomes-focused. Under this approach, supervisors could achieve the desired goals of policyholder protection and insurer solvency without the costs that would result from implementing new global systems in nearly every country in the world.

Unfortunately, the IAIS does not seem to be heading in this direction. Implementation of the ICS may require adopting different accounting standards and the global capital requirement may favor the local approach of one jurisdiction over another, creating further disproportionate costs between similarly situated companies. The potential market disruptions could be unintended, but very significant. Additionally, it appears that the IAIS is moving forward without a full assessment of the impact on U.S. consumers and insurance markets.

The FSB Structure and Process

The Plenary of the FSB is the sole decision-making body of the board and it operates on the basis of consensus, not actual voting. That, however, is largely all that is known about the decision-making process at the FSB, and there is no formal process for communicating NAMIC members' concerns to the U.S. representatives on the FSB. Further, the Plenary is dominated by central banks and political appointees. Consequently, there is ample reason to doubt that the Board fully understands how its decisions affect insurance markets, or that the critical differences between banking and insurance are fully appreciated. And yet, the decision to craft a new global consolidated capital standard for all IAIGs was made by an organization that has no insurance expertise from the U.S. and little expertise from other countries other than the IAIS representatives that report to them. The U.S. is represented on the FSB by the Treasury Department, the Federal Reserve, and the Securities and Exchange Commission. Interestingly, there are no U.S. state insurance regulators or lawmakers represented on the FSB.

Finally, it is important to note that neither the FSB nor the IAIS are bound by due process and neither formally considers the costs of the changes they are making to international insurance standards relative to the presumed benefits of these changes. With each new or revised standard, costs are added from international regulatory

enforcement and compliance with seemingly little regard for the impact of these costs on governments, insurers, and consumers.

Conclusion

NAMIC believes it is important to ensure that federal agencies representing the U.S. on the FSB and at the IAIS are advancing policy positions that represent the interests of U.S. insurance consumers, insurance markets, insurance regulators, and the U.S. economy in general. To that end, the U.S. should insist on an open and transparent policy development process, and the U.S. representatives who engage with international bodies should share a common agenda and a common message. That message should include a strong defense of the U.S. insurance market and existing regulatory structure. It should also promote the interests of U.S. insurers and their policyholders.

Congress has a critically important role to play as these international discussions continue. Through oversight and awareness, along with the possible enactment of legislation to facilitate a needed course correction if necessary, lawmakers can help protect the robustly competitive insurance market in this country. NAMIC applauds the Committee for holding this important hearing.