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THE IMPACT OF INTERNATIONAL REGULATORY STANDARDS ON THE COMPETITIVENESS OF U.S. INSURERS—PART II

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND INSURANCE

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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THE IMPACT OF INTERNATIONAL REGULATORY STANDARDS ON THE COMPETITIVENESS OF U.S. INSURERS—PART II

Thursday, February 25, 2016

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING
AND INSURANCE,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:01 p.m., in room 2128, Rayburn House Office Building, Hon. Blaine Luetkemeyer [chairman of the subcommittee] presiding.

Members present: Representatives Luetkemeyer, Royce, Garrett, Pearce, Posey, Stivers, Ross, Barr, Rothfus, Williams; Cleaver, Green, Moore, and Beatty.

Ex officio present: Representatives Hensarling and Waters.

Also present: Representative Duffy.

Chairman LUETKEMEYER. The Subcommittee on Housing and Insurance will come to order. Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers–Part II."

Before we begin, I would like to thank the witnesses for appearing before the subcommittee today. We look forward to your testimony. I now recognize myself for 3 minutes to give an opening statement.

This subcommittee has spent a great deal of time focusing on international factors affecting our domestic insurance markets. Today's hearing provides an opportunity to hear from the industry firsthand on implications, both positive and negative, stemming from international insurance standards and agreements.

Today's hearing will also focus on draft legislation that would create a more formalized role for congressional monitoring of these standards and agreements. This legislation has been drafted with the input of a wide variety of stakeholders, and today's testimony will help to improve the bill before it is introduced.

Legislation discussed today would establish a series of reasonable requirements to be met before Treasury's Federal Insurance Office (FIO), the Federal Reserve, or any other party to these international conversations could consent to the adoption of any final insurance standard. Similar standards would be set for negotiations

on covered agreements, including the covered agreement currently being negotiated with the European Union.

The draft also outlines a more robust role for the FSOC independent member with insurance expertise, strengthening Team USA in its ability to advocate for policies that suit U.S. insurance markets and consumers.

This bill is not intended to bring the international process to a grinding halt. Team USA has experienced victories at the International Association of Insurance Supervisors (IAIS) and has kept this body informed of its intent to negotiate the first of what could be many covered agreements. We should not underestimate the importance of these conversations or the implications that they have on insurers. The higher loss absorbency draft rule and lingering questions around temporary equivalency for U.S. insurers conducting business in the European Union have demonstrated that the United States hasn't always ended up with the best deal.

It is imperative that the United States, that is the States, the Executive Branch, and Congress work cooperatively to signal to the IAIS, the Financial Stability Board, and foreign governments that we will only lend our name to standards and agreements that benefit U.S. consumers and allow us to maintain a robust insurance marketplace.

This draft legislation aims to do just that. It will provide greater transparency, allow for a stronger Team USA, and indicate to foreign bodies the United States will lead and not be led.

I thank our distinguished panel for being here today. We look forward to your testimony and your comments about the discussion draft.

The Chair now recognizes the ranking member of the subcommittee, the gentleman from Missouri, Mr. Cleaver, for an opening statement.

Mr. CLEAVER. Thank you, Mr. Chairman. Chairman Luetkemeyer, members of the subcommittee, I would like to begin by thanking our witnesses for their appearance here today. Today's hearing, "The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers–Part II," is an opportunity for an additional look at the insurance standards that are being developed on an international level through the U.S.'s participation in the International Association of Insurance Supervisors and the Financial Stability Board (FSB).

Following the financial crash of 2008, the passage of the Dodd-Frank Act created the Federal Insurance Office (FIO). FIO has been tasked with coordinating Federal efforts and developing Federal policy on prudential aspects of international insurance matters, including representing the United States in the IAIS. FIO, along with the National Association of Insurance Commissioners (NAIC), and the Federal Reserve has been serving as the U.S. representatives to the IAIS. It is important to note that no standard agreed to internationally is binding on the United States unless adopted domestically.

Our witnesses today will provide the subcommittee with their perspective on how the discussions on the international level are proceeding. As members of this subcommittee, it is important that we remain focused on the work being done internationally to en-

sure transparency and stakeholder input. I look forward to the hearing and their insight.

Thank you, Mr. Chairman. I yield back.

Chairman LUETKEMEYER. I thank the gentleman.

The Chair now recognizes the gentleman from California, Mr. Ross, for 2 minutes for his opening statement.

Mr. ROSS. Thank you, Mr. Chairman, and let me say at the outset that I share the stated goals of increasing transparency and accountability in international regulatory discussions. I think we should also be looking at governance and transparency reforms in domestic regulatory decision-making.

I am concerned, however, that Congress may be exporting the State versus Federal turf war into the international arena to the detriment of U.S. companies and consumers. We are at a watershed moment in international insurance regulation.

The United States has much to gain by moving forward with a covered agreement on reinsurance collateral with the E.U. Formal negotiations would give the United States leverage in discussions about equivalency under the European Solvency II regime. Simply put, without action, U.S. companies lose. They are either cut out of the European market or they are forced to post billions in additional capital, which is then unavailable to invest in the United States or to invest in emerging markets.

Reforming arbitrary and discriminatory State reinsurance collateral laws through a covered agreement has been a bipartisan goal of this committee since 2010. Representative Kanjorski, the architect of the key language that we put into Dodd-Frank, on this said that, "Covered agreements and pre-emption were designed to harmonize reinsurance standards across national borders." That was the goal.

These covered agreement negotiations, I might add, are already subject to substantial congressional oversight, including a 90-day layover period, so there is little we need to fear in terms of a lack of transparency.

In conclusion, Mr. Chairman, there is widespread agreement on the issues related to domestic capital standards and increased transparency in international negotiations. And respectfully, if we are going to move legislation, we should stick to those issues and ensure that we are not intruding on the important covered agreement negotiations already taking place.

Thank you again, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman yields back.

We will now yield 2 minutes, or whatever time she may consume, to the ranking member of the full Financial Services Committee, the gentlelady from California, Ms. Waters.

Ms. WATERS. I thank you, Mr. Chairman, and I would like to welcome our witnesses. We are here today to discuss the United States' participation at international standard-setting organizations and our efforts to prevent another global financial crisis. I applaud this work, and I look forward to continued collaboration on these issues.

Dodd-Frank included several changes to help us prevent the possibility of a future collapse of large, globally active insurance companies like AIG. In particular, Dodd-Frank created the Financial

Stability Oversight Council, known as FSOC, an entity that for the first time is responsible for examining risks facing our entire financial system.

The FSOC has authority to designate non-bank financial companies after thorough consideration of several factors including, but not limited to, insurance companies for enhanced supervision. Congress likewise gave regulators the authority to require enhanced standards for these non-bank firms accounting for the fact that the business model of insurance companies may demand a different regulatory response.

Dodd-Frank also lays out the Federal Government's role in coordinating a U.S. response to international issues and developing Federal policy on prudential aspects of international insurance matters. These authorities were all enacted with one goal in mind, to protect financial stability and prevent the next financial crisis.

I believe that our State-based regulatory system certainly has its strengths. The California Insurance Department does particularly good work and tends to set a high standard for the protection of policyholders.

But I also strongly support the reforms provided by Dodd-Frank to fill important gaps in oversight and increase collaboration by ensuring that we are looking at the big picture, both domestically and internationally. We can help ensure long-term financial stability while also strengthening consumer protections as we continue to learn more about potential risks that insurers can pose to national and global financial stability. I look forward to continuing our conversation so that we can be sure we do not repeat the mistakes of the past.

So I thank you, Mr. Chairman, and I will yield back the balance of my time.

Chairman LUETKEMEYER. The gentlelady yields back. Before we get started, I just want to explain what is going on here. We anticipated having some votes shortly, but they have been postponed now until 3:00, I understand, so we will continue to go as far as we can. And as soon as they call votes, we will take a recess.

I understand that they are looking at probably an hour for votes. And after the completion of those votes, we will come back and continue our hearing.

So with that, let me welcome the witnesses today: Mr. Gary Thompson, president and chief executive officer of Columbia Insurance Group, on behalf of the National Association of Mutual Insurance Companies; Mr. David Zaring, associate professor, Department of Legal Studies and Business Ethics, The Wharton School; Mr. Joseph Torti, III, vice president for regulatory affairs, Fairfax, Inc., on behalf of the Property Casualty Insurance Association of America; and Ms. Carolyn Cobb, vice president and chief counsel for reinsurance and international policy, the American Council of Life Insurers.

Each of you will be recognized for 5 minutes to give an oral presentation of your written testimony. And without objection, your written testimony will be made a part of the record. A quick tutorial on the buttons in front of you: green means go; yellow means you have a minute left; and red means you are out of time.

Mr. Thompson, my fellow Missourian, living just a few miles up the road, in fact, from where I live, thank you very much for traveling all the way to D.C. You are recognized now for 5 minutes.

STATEMENT OF GARY THOMPSON, PRESIDENT AND CHIEF EXECUTIVE OFFICER, COLUMBIA MUTUAL INSURANCE COMPANY, ON BEHALF OF THE NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES (NAMIC)

Mr. THOMPSON. Good afternoon, Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee. Thank you for the opportunity to speak to you today.

As you said, my name is Gary Thompson and I am president and chief executive officer of Columbia Mutual Insurance Company, a mid-sized regional company headquartered in Columbia, Missouri. We are an insurance group which does business in 14 States and is licensed to do business in 22 States. For over 140 years, it has been our mission to build enduring relationships with our customers by providing value and exceptional service and fulfilling our promises.

I am also here today in my capacity as a member of the board of directors of the National Association of Mutual Insurance Companies. NAMIC is the largest property and casualty insurance trade association in the country with more than 1,400 member companies representing 40 percent of the U.S. property and casualty insurance in the marketplace.

Both Columbia and NAMIC are very appreciative of this subcommittee's focus on international insurance issues and commend Chairman Luetkemeyer's efforts in crafting this discussion draft legislation.

We have serious concerns about recent efforts to create international regulatory standards for insurance companies and believe Congress should conduct strong oversight in this area in order to protect domestic insurance markets, companies, and especially policyholders. We need lawmakers to weigh in on the debate on the side of defending the existing State-based regulatory structure that we know to be time-tested and strong.

Since the financial crisis, the G20 Financial Stability Board and the International Association of Insurance Supervisors have become increasingly engaged in regulatory standard-setting for insurance companies ostensibly in the interest of providing global financial stability and regulatory harmonization. The primary example of this is the IAIS work on a new global capital standard for internationally active insurance groups.

Today, we have heard no real justification of a need for this type of one-size-fits-all standard and are skeptical of regulation uniformity for uniformity's sake. We need our country's officials who engage in these international conversations to speak in defense of the U.S. market, existing regulatory structure, insurers, and especially policyholders.

Columbia is not an internationally active insurer, but our company and companies like ours are concerned about forcing uniformity across very different regulatory environments with very different economic and political goals. The chief concern is the eventual importation of foreign regulatory standards for all companies

which supplant or duplicate existing standards that we know to be effective and which have served our consumer and insurer needs for more than a century.

Congress has a critically important role to play in helping ensure that the United States is appropriately represented in these international discussions. Given the direction of many of the conversations at the IAIS, we believe that legislation is not only timely and appropriate, but necessary. Any legislation must make clear that our existing State-based regulatory system is effective and must be defended and preserved.

We believe the discussion draft legislation represents a good starting point. In my written statement, I have provided a detailed section-by-section analysis of the many positive provisions currently included in the bill. However, I would like to highlight what we see as the necessary improvements to further strengthen the bill before introduction.

First, the bill needs to clearly acknowledge that any international standard is not self-executing and is entirely without legal effect in the United States until implemented through a Federal or State legislative or regulatory process. Clear language to this effect should be added.

Given that the outcomes of these international standard-setting discussions are not binding, a second addition should include language that prevents participating Federal officials from agreeing to any standards which would require any additional changes to current State or Federal law.

These international organizations have no legal authority and our officials have no business even appearing to obligate the United States to any standard that does not conform to laws and regulations established here at home.

Finally, we urge the committee to include covered agreements under the guidelines and processes laid out in the discussion draft. Covered agreements have unprecedented authority that will preempt State law and could be used as a back channel to alter insurance regulation in this country. These agreements are absolutely in need of robust monitoring, stakeholder input, and congressional consultation on direction.

As we move forward, NAMIC stands ready to work with the committee to include what we see as necessary improvements to the discussion draft. Again, thank you for the opportunity to speak here today, and I look forward to answering any questions you may have.

[The prepared statement of Mr. Thompson can be found on page 51 of the appendix.]

Chairman LUETKEMEYER. The gentleman yields back.

With that, Mr. Zaring, you are recognized for 5 minutes. You may begin.

STATEMENT OF DAVID ZARING, ASSOCIATE PROFESSOR, LEGAL STUDIES AND BUSINESS ETHICS, THE WHARTON SCHOOL, UNIVERSITY OF PENNSYLVANIA

Mr. ZARING. Good afternoon, and thank you for having me. I am an associate professor of legal studies and business ethics at The Wharton School. I study financial regulation and in particular

international financial regulation, a field of growing importance and one that has already transformed the way that banks and capital markets are regulated. It is a field of increasing importance to insurance as well.

In my testimony today on international cooperation in insurance standards, I would like to focus on three points. The first is that international financial regulatory standards protect American consumers and American financial stability in two ways. International standards create a level playing field for financial market participants when they expand their businesses abroad and can also prevent disruptive financial contagion that starts elsewhere from affecting the American marketplace.

Until recently, international insurance regulation was a relatively quiet field, but in the wake of the financial crisis that has changed. And we should generally welcome the new vibrancy in institutions like the Financial Stability Board and the International Association of Insurance Supervisors in creating consistent capital standards and supervisory approaches for insurance companies, many of whom do business at home and abroad.

Second, it is important to remember that the United States has traditionally played a very strong role in formatting and formulating standards in matters of international regulatory cooperation, a role that would be threatened by legislation that ties the hands of its representatives.

American regulators have substantially increased the degree of transparency of the international efforts to develop common capital standards for banks. They have also had a very large say in the sort of capital standards chosen. And they have set the terms of regulatory cooperation by capital markets overseers. It could hardly be otherwise given the size and strength of the American economy.

On the other hand, where American regulators have not fully engaged in the international process they might find themselves in a position where they must later accept standards that have been designed without their input, as the Securities and Exchange Commission has come perilously close to finding with regard to the development of international accounting standards.

It is all but assured that representatives who represent everyone engaged with the domestic insurance industry would play a critical role in international insurance regulation given the size, strength, and importance of the American insurance market. But if their ability to negotiate is curtailed, or if there are too many voices at the table, then their influence will likely also be curtailed and confused as well.

Third, while the importance of a transparent and open administrative process is undoubtedly significant, the best sort of transparency and democratic accountability is provided by legislative authorization to engage in international negotiation at the beginning of the process followed by domestic implementation through regular administrative procedure at the end of it.

No global terms will be imposed upon American insurers until American regulators adopt capital or other rules through notice and comment on a State-by-State basis, subject to State administrative law or by the Federal Reserve, subject to Federal administrative law.

In the past, American regulators have tailored international standards to meet the needs of the American market. The Federal Reserve, for example, came up with a two-stroke procedure for implementing the second iteration of the Basel Capital Accord.

In my view, it is important to remember that nothing binds American consumers or market participants until American regulators come home and go through the traditional rulemaking process with notice and comments.

Attempting to add a new set of procedural obligations on top of this to the middle of a process that begins with congressional authorization and ends with domestic notice-and-comment rulemaking, would likely be both burdensome and counterproductive.

In particular, forcing regulators to repeatedly hold notice and comment both before and during their international negotiations is a bad way to negotiate effectively. And just as no business or agency opens every meeting or deliberation to any shareholder or stakeholder who wants to show up, it is difficult to see why international standard-setters would benefit from a process where every meeting was open to observation by anyone at any time.

I look forward to your questions.

[The prepared statement of Mr. Zaring can be found on page 67 of the appendix.]

Chairman LUETKEMEYER. Mr. Torti, you are recognized for 5 minutes.

STATEMENT OF JOSEPH TORTI, III, VICE PRESIDENT, REGULATORY AFFAIRS, FAIRFAX FINANCIAL HOLDINGS LIMITED, ON BEHALF OF THE PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA (PCI)

Mr. TORTI. Thank you, Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee. My name is Joe Torti. For 13 years, I was the Rhode Island superintendent of banking and insurance. I am now the vice president of regulatory affairs for Fairfax, testifying on behalf of the Property and Casualty Insurers Association of America (PCI).

Fairfax is a diversified international company that includes insurance operations that write everything from Main Street business in the United States to Odyssey Re that provides reinsurance to risk located in more than 100 countries. PCI represents nearly 1,000 insurers and reinsurers in the United States and around the globe.

PCI supports the subcommittee's efforts to draft consensus legislation clarifying congressional intent on insurance regulation and international representation. We appreciate and support the chairman's ongoing leadership and improving legislative drafts.

Congress, in the Dodd-Frank Act, affirmed the State-based regulation of insurance and the McCarran-Ferguson Act in support for the States' historic focus on consumer and policyholder protection. But there have been a number of emerging gray areas as the new regulatory roles have evolved where additional congressional clarity could be very helpful.

I can tell you from personal experience as both a bank and insurance regulator that the two supervisory perspectives can be dramatically different, for examples, on issues such as capital

leveraging and liquidity risk or the more holistic issues of macroeconomic stability versus policyholder protections.

Congressional oversight has been very helpful to the evolving U.S. process, particularly in encouraging regulatory cooperation and transparency. By working towards bipartisan legislation, Congress can help ensure that our Team USA regulators have the same priorities and objectives and greater congressional clarity in carrying out their missions.

This in turn will improve the likelihood of efficient and effective outcomes in international insurance regulatory deliberations. PCI therefore appreciates the interest and leadership by Chairman Luetkemeyer and the members of the subcommittee and full committee towards that end.

For nearly 150 years, the States have regulated insurance and coordinated their activities through the National Association of Insurance Commissioners. As a former chief regulator from the State of Rhode Island, I know what effective regulation requires and how very well my State colleagues have done, including during the last financial crisis.

This success is not just an accident. The U.S. insurance regulatory system has been so successful because it focuses upon the end user, the consumer. So we strongly support congressional emphasis on the importance of putting consumer protection first, as does our State-based regulatory system.

In recognition of this strong performance of State regulation, Dodd-Frank reiterated the primary supervisory role of the States. However, it also created the Federal Insurance Office (FIO) in the Treasury and gave the Federal Reserve Board limited regulatory authority over certain categories of insurers.

Unfortunately, without more congressional guidance on their objectives and priorities, our U.S. and State representatives can have conflicting perspectives and priorities. For example, FIO, the Federal Reserve, and State regulators took divergent actions on whether to eliminate consumer group and stakeholder involvement in IAIS working groups. Both transparency and accountability have since suffered. It is important that the United States be at the table, but it is equally important that our representatives be on the same page.

Accordingly, we support congressional clarity to encourage greater collaboration and consensus among regulators and to reverse the trend towards closing doors to consumer groups and other public stakeholders. PCI particularly supports a united effort in the negotiation of international covered agreements.

The European Union's new regulatory system that they are beginning to implement, Solvency II, requires discriminatory regulation against insurers and reinsurers from third countries unless the third country is deemed to be equivalent, a highly prescriptive process.

We are pleased that the Treasury and USTR have indicated that they will push for recognition of U.S. regulation by the E.U. in connection with their discussions with the E.U and do not intend to exceed their negotiating authority with respect to agreeing to domestic regulatory changes. Mutual recognition is a critical priority

for Fairfax to avoid discrimination. We appreciate the congressional encouragement towards that goal.

In conclusion, the international insurance regulatory world has evolved in ways that may not reflect congressional intent to support the strength and competitiveness of the U.S. insurance market and its consumer-focused State-based regulatory system.

PCI commends this subcommittee for your efforts to date and urges committee members to work together towards bipartisan consensus on the Luetkemeyer draft and similar efforts to clarify congressional intent and improve international insurance regulatory deliberations and outcomes.

I look forward to your questions.

[The prepared statement of Mr. Torti can be found on page 62 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Torti.

And Ms. Cobb, you are recognized for 5 minutes.

STATEMENT OF CAROLYN COBB, VICE PRESIDENT AND CHIEF COUNSEL, REINSURANCE AND INTERNATIONAL POLICY, AMERICAN COUNCIL OF LIFE INSURERS (ACLI)

Ms. COBB. Thank you, Mr. Chairman. Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee, my name is Carolyn Cobb. I am vice president and chief counsel of reinsurance and international policy at the American Council of Life Insurers. I am pleased to present this statement on its behalf.

Life insurers are essential to helping families achieve retirement security. Guaranteed lifetime income solutions provided by life insurers are the building blocks of secure retirement. Life insurers investments are also a powerful source of long-term capital and economic growth.

That is why the development of international capital standards by the Federal Reserve Board and the International Association of Insurance Supervisors could have a significant impact. These standards must be appropriate for insurers, and they must be consistent with the long-term horizon of life insurance products that provide guarantees lasting many decades.

This committee and the entire Congress affirmed this principle by unanimously passing the Insurance Capital Standards Clarification Act of 2014. ACLI thanks the chairman, the ranking member, and this committee for your strong leadership in support of that legislation. It gave the Federal Reserve Board flexibility to tailor an insurance capital standard to the insurance business model.

ACLI commends the Fed for its plan to conduct formal rulemaking with notice and public comment and for its many public statements, including before this committee, that it intends to exercise the discretion authorized by Congress to tailor capital standards for insurance companies.

The Board's domestic process, however, cannot be rushed or confused by the development of international capital standards. The United States should conclude its process before agreeing to any international standards. This sequencing is critically important. It will equip Team USA with a strong unified position in any IAIS or FSB discussions and so will be more likely to have the best out-

come. We want the Fed's process to inform the IAIS and not the other way around.

U.S. Federal agency leadership by Treasury and the Fed, in strong partnership with our State insurance regulators, is more important than ever before. The full involvement of Treasury and the Board in FSB and IAIS discussions and decisions is essential to influencing the international process and to ensuring those standards reflect the unique strengths of the U.S. system for insurance regulation. Any restriction, even inadvertent, on the ability of Team USA to participate in international standard-setting organizations would in no way protect U.S. insurers or U.S. insurance consumers.

We are also concerned that the IAIS is currently treating certain types of annuities as systemically risky. They are called variable annuities. They provide guaranteed income in retirement. These products have been approved and regulated by our State supervisors. They have provided retirement income to U.S. consumers for over 60 years. They must not be placed at a competitive disadvantage by international capital standards.

The principle should be that all insurance products, whatever their country of origin, if they have similar risk characteristics, they should be treated the same. We appreciate Team USA's continued focused attention to this concern.

ACLI commends Chairman Luetkemeyer and other members of the committee for their development of the discussion draft. It reflects the principles of transparency, accountability, and due process that ACLI supports. It improves congressional oversight over international standard-setting initiatives and expresses clear objectives for them, maintaining the ability of the U.S. insurance industry to offer the products on which U.S. consumers rely. These important goals are shared by ACLI.

ACLI would suggest some refinements to the discussion draft for the committee's consideration. They will be consistent with the view that any restriction on the ability of Team USA to participate fully at international standard-setting organizations would be harmful to U.S. interests.

ACLI thanks the committee for its leadership on this legislation and looks forward to working with it on suggested changes.

Thank you, Mr. Chairman, for holding the hearing. I appreciate the opportunity to testify and look forward to questions.

[The prepared statement of Ms. Cobb can be found on page 38 of the appendix.]

Chairman LUETKEMEYER. Thank you, Ms. Cobb. You all did a great job. Everybody came in under time. Thank you very much.

Let me begin the questioning this afternoon with probably an opening comment in that there is a lot of interest and a lot of concern with regards to our ability to negotiate and what is being negotiated at the international level. And this is the reason why we are here this afternoon. That is the reason for the bill.

I have had multiple Members come to me with concerns and so we have tried to draft something that addresses a lot of their concerns as well as listen to the concerns of the industry and continue to work with you as this is a draft, and we want to continue to listen to your concerns.

So let me begin first by asking a question. All of you seem to have answered it, but I want to put you on record because I think it is important. Do you believe we need a FIO or to have someone representing the United States at these international discussions?

Mr. Thompson?

Mr. THOMPSON. Yes, we do.

Chairman LUETKEMEYER. Mr. Zaring?

Mr. ZARING. Yes, we do.

Chairman LUETKEMEYER. Mr. Torti?

Mr. TORTI. Yes, we do, with the support of State regulators.

Chairman LUETKEMEYER. All right.

Ms. Cobb?

Ms. COBB. Yes, we do.

Chairman LUETKEMEYER. You mentioned it multiple times in your discussions, but it is a formality, and I need to get that on record.

We also have an independent member that we also address in our bill that is a member of FSOC, which really doesn't have a lot of input but we believe needs to be a participant in the process at IAIS discussions. Do you believe that it is important that that member also be at the table?

Mr. Thompson?

Mr. THOMPSON. Yes, sir, it is absolutely critical, as that individual is really the only individual with really deep insurance knowledge to lend itself to those discussions, so absolutely yes.

Chairman LUETKEMEYER. Thank you.

Mr. Zaring?

Mr. ZARING. I think that voting role can be filled by the Federal Insurance Office and having too many American representatives at—

Chairman LUETKEMEYER. Yes. Our bill doesn't give him a voting role, really. It just gives him a participant role where he can be at the meetings, which he cannot be in right now.

Mr. ZARING. No, no, I mean, his voting role on FSOC, but maybe I should be clear. I think the Federal Insurance Office representative who Chairs the head of the office as a whole can do a sufficient job in representing American interests in a coordinated way without the input of the member, which I am sure he gets anyway.

Chairman LUETKEMEYER. Mr. Torti?

Mr. TORTI. I believe the independent expert plays a critical role and should have a participatory participation in the process.

Chairman LUETKEMEYER. Okay.

Ms. Cobb?

Ms. COBB. The independent member has made significant contributions to discussions at various levels. We have not concluded our review of that portion of the bill.

Chairman LUETKEMEYER. Okay. Thank you. Mr. Thompson, you had a couple of different comments which we have a clause or a section of this that discusses covered agreements. We also have a section in your written testimony where you talk about concerns about the cost-benefit analysis, and I think we also have that covered in our bill.

Do you not believe that we covered it adequately in our bill? Do you want to expand it or what are your concerns? Or did you not see those portions that I think we had covered in there?

Mr. THOMPSON. Yes. As we said, Mr. Chairman, we think the bill goes a long ways, and we did suggest a couple of what we view as improvements of that and particular language around this issue of covered agreements. We absolutely think that there is a place for covered agreements. Don't misunderstand. And that U.S. negotiators should be at the table discussing those.

But we also believe that should be done in a very transparent process because our concern is that they do have that unprecedented power to exempt State law. And without the proper oversight and regulatory process, we are concerned that those such agreements could be in conflict with State laws.

Chairman LUETKEMEYER. One of the things that we want to try and do, and we have been discussing and it hasn't completely gotten itself into the draft yet, it was a way for Congress to be able to approve those commitments that are made by the FIO Director. I think it is important that there is somebody on this side of the pond to be able to give a yes or no or thumbs up on some of this stuff without—we don't want to gum up the system.

But by the same token, I think part of our job here in Congress is not just to legislate but to provide oversight, because all four of you asked for us to do that in your testimony today. And so I think it is something that we need to do is to be able to be—and in your situation, Mr. Thompson, when you talk about the covered agreements also sort of pre-empting State law, I think we need to have somebody here on this side of the pond to be able to say, hey, we believe this is a good deal or a bad deal and be able to say thumbs up or thumbs down.

So I guess my question is, do you believe that Congress needs to be involved in sort of approving the agenda or whatever comes out of the negotiations with the FIO Director?

Mr. THOMPSON. Yes, sir, we do. And that is the suggestion we spelled out in my written testimony for the committee to consider. It is a process by which that would do it. Not to delay the process, but to simply do as you suggest, Mr. Chairman, to bring those out so that there is an opportunity to review those to make sure there is not conflict with State law. And if there is, a process then that can be resolved to address those conflicts.

Chairman LUETKEMEYER. Mr. Zaring, do you agree with that? I am running out of time. Please, yes or no?

Mr. ZARING. I don't think I agree with that as things stand right now, though I know the process is evolving.

Chairman LUETKEMEYER. Okay.

Mr. Torti, do you think Congress should be able to approve or disapprove those actions to make sure that they are not in conflict with what goes on over here?

Mr. TORTI. Yes, I do.

Chairman LUETKEMEYER. Ms. Cobb?

Ms. COBB. We need a covered agreement with the European Union and the current law gives Congress the power to reject it.

Chairman LUETKEMEYER. Okay. Thank you very much. My time has expired.

I yield to the ranking member of the subcommittee, Mr. Cleaver from Missouri, for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman. Thank you for your questions. When you look at all of the multiple bills that have been submitted here in the House, and I am sure you have read all of them instead of probably watching movies but how are we going to strike a balance in terms of transparency and accountability?

Mr. Torti, you know, we don't get what we really want in negotiations. We get what we negotiate. And so I am wondering, number one, should our negotiators have flexibility as they are sitting down? And number two, it is just the same question about chronic accountability. How do we strike a balance between encouraging transparency and accountability and then overly narrowing our negotiators' ability?

Mr. TORTI. I think we can strike that balance. It is very important that we be granted, that the United States be granted equivalency, that the U.S. system be seen as equivalent to Solvency II in order for us as the insurance industry to have a competitive environment and to be able to compete with European Union companies.

Closing working group meetings where the stakeholders, the insurance industry and consumers are not allowed to witness the deliberations could lead to a conclusion or a standard that perhaps is not appropriate or not the best standard for protection of consumers or in the best interests of a competitive marketplace.

So I think you can strike that balance. There is a process here where your congressional hearings are all open to the public and very transparent and it just doesn't work that way at the IAIS. And it is very opaque and as stakeholders we need to be at the table and be able to witness what type of deliberations are going on and what type of decisions are being made. And I think our input would add greatly to the strength of the outcome of those deliberations.

Mr. CLEAVER. I have a friend who is a Federal judge, and he says the worst thing that has ever happened to the judicial process in this country was bringing television cameras into the courtroom, that you get a production instead of a trial. I am for the transparency, but I am just struggling with, how do you ensure transparency without inhibiting the negotiations?

Yes, sir, Mr. Thompson?

Mr. THOMPSON. Mr. Cleaver, if I may add to Mr. Torti's comments to respond to that, you said at the beginning that oftentimes in negotiations neither side gets exactly what they wanted when they get there, and I completely agree with that. As a business man I have entered into numerous negotiations and walked out very much the same way.

Mr. CLEAVER. Don't run for Congress.

[laughter]

Mr. THOMPSON. That is why we think this draft legislation is very important because it sets forth those guidelines to Team USA, the Fed and FIO particularly, so that they know what can be negotiated and frankly what cannot be negotiated. So it will allow them to focus on those items or areas of negotiation which they should be allowed to negotiate with.

But yet this committee in this draft legislation sets boundaries or guidelines around what is off the table, and we think that is a very helpful process to the negotiation process.

Mr. CLEAVER. Ms. Cobb?

Ms. COBB. A covered agreement, which I think is what you are asking about, is essential to protect the competitiveness of U.S. insurers. And in my view, and I have read that statute many times. I don't believe that it can be used to import international standards. So FIO and USTR have given you a fairly specific list of things that they want to negotiate for the benefit of U.S. insurers.

This is our first try at a covered agreement. It is an essential tool for the U.S. insurers to ask their Government to use to reduce conflict among regulators in different countries. So I think given the notice that you have had, given that you get to say no thank you, and given how much the industry needs this covered agreement, my view is let us see how it works.

Mr. CLEAVER. I yield back, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman's time has expired.

With that, we will go to the gentleman from California, the chairman of the House Foreign Affairs Committee, Mr. Royce, for 5 minutes.

Mr. ROYCE. Thank you again, Mr. Chairman. Mr. Torti, I have some questions for you as a reformed insurance commissioner and much to my chagrin, and I assume yours as well, the NAIC hasn't prioritized collateral reform. And that is what I wanted to talk to you about because in 2011, the NAIC certified the reinsurer provisions. They are still not an accreditation standard. A long time has passed and a third of States haven't modernized their laws, including major States like Texas and Illinois.

Moreover, States who have modernized their reinsurance laws have not done so in a uniform fashion, unfortunately. So Mr. Torti, in November of 2014 you told NAIC's Reinsurance Taskforce that you believed that uniformity is an important consideration and that this should be taken to the accreditation committee for further discussion.

But then NAIC testified to us last September that it was going to in November start the conversation about accreditation for credit for reinsurance—"That is a hammer we have." So with the model passed in 2011, seasoned 3 years, then referred to by you as an important consideration in 2014, shouldn't the accreditation conversation have been finished rather than beginning in 2015? And why didn't the NAIC listen to you and go forward and prioritize this?

Mr. TORTI. Thank you for that question, Congressman. I just want to clarify I no longer represent the NAIC. I cannot speak for the NAIC at—

Mr. ROYCE. But you can speak as a former regulator. I am just trying to get to a point.

Mr. TORTI. I can explain the accreditation process and I can give you just a very brief description of why, in 2011, it wasn't immediately ratified or considered to be an accreditation standard. Generally, the way the accreditation program works is that if a State implements a more stringent requirement than the accreditation requirement, it is in compliance with the accreditation program.

But prior to the implementation of the new credit for reinsurance standard 100 percent collateral was the standard which was considered to be a higher standard than the—

Mr. ROYCE. Okay. Let me ask you this, then. Given NAIC's inability to act in the 6 years since Congress made this a priority, I assume you now support Treasury negotiating a covered agreement on collateral and using this as leverage in the equivalence discussion?

Mr. TORTI. I do support equivalency and mutual recognition being the primary concern in the covered agreement discussions. It is absolutely necessary as an industry that we attain equivalency so that we are not disadvantaged—

Mr. ROYCE. Right. But do you—

Mr. TORTI. —when operating—

Mr. ROYCE. Do you support Treasury negotiating that covered agreement?

Mr. TORTI. I do.

Mr. ROYCE. Okay.

Now, I would like to go to Ms. Carolyn Cobb, vice president and chief counsel, reinsurance and international policies. Ms. Cobb, the purpose of this hearing is to examine whether international regulatory standards might be harmful to U.S. insurers. I would like to clarify that I do not consider the new covered agreement negotiations to be an imposition of an international regulatory standard but rather a bilateral discussion about removing barriers or potential barriers on both sides of the Atlantic and an acceptance of each other's domestic supervision.

Indeed, my understanding is that the U.S. insurance industry broadly favors pursuing the agreement because it is aimed at resolving the equivalence issue under Solvency II to the benefit of U.S. insurers operating in the E.U. Is that a fair statement in your opinion, and does ACLI support the covered agreement negotiations?

Ms. COBB. Yes, it is a fair statement. We support the negotiation of a covered agreement. Our board asked that State insurance regulators be included in those discussions, of course, as our prudential supervisors.

Mr. ROYCE. I thank you.

Mr. Chairman, I yield back.

Chairman LUETKEMEYER. The gentleman yields back.

The gentleman from Texas, Mr. Green, is recognized for 5 minutes.

Mr. GREEN. I will reserve and be heard later.

Chairman LUETKEMEYER. Okay.

We will go to Ms. Moore, from Wisconsin. She is recognized for 5 minutes.

Ms. MOORE. Thank you, Mr. Chairman, and thank you, Mr. Ranking Member. I also want to thank the witnesses for coming here this afternoon. Let me start out with you, Mr. Thompson. I was looking at your testimony from the Property Casualty Insurers and just need some clarification.

You say that when we did the Dodd-Frank Act, we abolished the Office of Thrift Supervision, which was kind of a culprit in dropping the ball in terms of their regulatory authority and transfer-

ring its authorities over the thrifts with insurance affiliates to the Federal Reserve and then created the office of FIO.

You go on to say that the State supervision is really good in that there ought to be coordination, but I guess what confuses me is that you speak about insurers not wanting any Federal regulatory framework, but it seems to me, if I am understanding your testimony, you almost say that given the three different approaches that you have from all of these supervisors, it is almost compelling us to move in that direction. I wanted you to sort of clarify what you were saying in your testimony.

Mr. THOMPSON. Congresswoman Moore, I apologize. You have referenced the Property Casualty Insurers of America, and I am not here representing them, so I want to—

Ms. MOORE. Oh, okay.

Mr. THOMPSON. I am representing the National Association of Mutual Insurance Companies, so I want to make sure I am responding to your question appropriately.

Ms. MOORE. Okay.

Mr. THOMPSON. And it is not intended for Mr. Torti? I'm sorry.

Ms. MOORE. Oh, I'm sorry. Mr. Torti is whom I need to respond.

Mr. THOMPSON. I am certainly happy to speak. I am certainly happy to speak to State—

Ms. MOORE. Okay. Mr. Torti, can you—I am so sorry.

Mr. TORTI. Would you mind just repeating the last part of that? I didn't catch it.

Ms. MOORE. Basically, you observed correctly that Dodd-Frank sort of shifted regulatory authority from the Office of Thrift Supervision, which we eliminated and gave part of it to the Federal Reserve and the other to the FIO. So it seems there is some sort of gap. But you still say that the State regulatory framework is the best one and that there is sort of a resistance for an overarching Federal regulation.

I guess I don't want to falsely conclude from reading this part of your testimony that you just sort of favor some sort of Federal insurance regulator.

Mr. TORTI. No, that is not the case. The intent of that statement was to make clear that the reference to the OTS and moving it over to the Federal Reserve, the part of AIG that did fail, the financial products division of AIG that did fail was an OTS-regulated part of that entity.

The insurance sector did very well during the financial crisis and the State regulatory system performed very well during the crisis, and that was the point of that section. It was not to say that there is a need for Federal regulation in any way.

Ms. MOORE. Okay. Well, thank you very much for that.

I guess I do want to ask Mr. Zaring, Professor Zaring a question about him signing on to the amicus brief in support of FSOC's final designation on MetLife. I guess I would like for you to give us a response. The critics will say that the process for designations and re-designations lacks clarity and transparency of insurance companies.

Mr. ZARING. Yes. I support the power of the FSOC to make the kinds of designation that it did in the case of MetLife. And I think it is a bad idea to impose too many fine-grained administrative

finding requirements on the council before it makes these designations, which are prudential in nature, involve macroeconomic forecasts that are difficult to reduce to costs and benefits and numbers.

And determining, say, a cost-benefit analysis or forcing the council to do something like that before engaging in a designation, I think just ties the council's hands and creates more risks for financial stability and designations that should have been made that weren't and fewer.

Ms. MOORE. My time has expired. Thank you.

Chairman LUETKEMEYER. The gentlelady's time is up.

With that, we go to the gentleman from New Mexico, Mr. Pearce, for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman. I appreciate each of you being here, and I would like to try to get a close view of just, say, one instance where regulation might disadvantage us, then take that up to the big view of looking back at the international standards and choices that might be made there and then come back to see what the effect might be on our consumers? And we are going to do that in 5 minutes, so okay.

[laughter]

So Ms. Cobb, I am on page six of your testimony where you talk about the short-term, yes, this is comments, okay, where you talk about the short-term view of assets by some of the regulators and the long-term nature of your products and then their value as cash equivalents or whatever the capital standards might be. Is that a fair assessment of your position?

Ms. COBB. Yes, sir.

Mr. PEARCE. Okay. So do you foresee anything that would come out of the international negotiations which would disadvantage your products? In other words, could the international discussion affect your ability to offer those products safely and in the fashion you have in the past?

Ms. COBB. With the caveat that the standards that are being developed internationally are not self-executing, right, they would have to be—

Mr. PEARCE. I understand. But let us say that they got executed.

Ms. COBB. Okay. So let us say they got executed. The principal—there are so many objections to the current version of it that I sort of don't know where to start, but one thing I want to call to your attention is that the current framework disadvantages variable annuities, as I said. And it has many other, I would say distortions, that need to be corrected.

Mr. PEARCE. So if I was reading your testimony correctly, that U.S. regulators have already described variable annuities as being subpar products. More or less, they don't favor those. Is that a correct interpretation of what you said?

Ms. COBB. U.S. regulators have approved variable annuity products. The international standard-setters believe they are systemically risky.

Mr. PEARCE. Okay. So there we are at the rub. So we are simply saying from here you all are contending—Mr. Zaring might take a different point of view—but basically the industry is saying, wait. They could do things over there and keep in mind that they are, the Europeans are implementing for countries like Estonia, like

Latvia, Bulgaria, do they have highly developed life insurance markets in those low-income States?

Ms. COBB. Not to my knowledge, Congressman.

Mr. PEARCE. Yes. So we have a completely different market here. And Mr. Zaring, with respect, you are saying that we should subjugate our market, which is highly developed. We have a lot of disposable income. We should not be bailed out. We shouldn't resist those efforts. We ought to just be there and then the fact that we are there almost implicates us to enforce those standards or we are bad faith negotiators. So how do we resolve that, Mr. Zaring? I see you want to speak. Go ahead.

Mr. ZARING. I would just say that what these international negotiations are supposed to result in is a modus vivendi between the European Union which has small undeveloped insurance markets but also markets served by Allianz and Generale and enormous global insurance companies and the way that American insurance companies do business and are scrutinized by regulators.

And the goal of things like the covered agreement and the international capital negotiations in general are to come up with a way that is acceptable for American regulators and regulators elsewhere in the world that let American insurance companies do business there and do business at home in a way that is consistent, that doesn't result in lots of regulatory differences between countries.

Mr. PEARCE. So I—

Mr. ZARING. And I think that the—

Mr. PEARCE. —get the drift of what you are saying. So what would cause me as a voter on the bill not to be concerned that we are going to have standards implemented which cause disadvantage to our industry and the ability of people to make a living and to ensure the future of the life, things which are not greatly concerned about when the income level reaches a low enough level like it does in some of the countries around the world? Why should I not be concerned about that?

Mr. ZARING. I would just say that first, we have done well in these sorts of negotiations in the past. And second, that anything we come up with has to go through notice and comment here, and that is the saving grace for domestic stakeholders who find that the international process has failed them.

Mr. PEARCE. With respect, as I close up and I appreciate that, I don't share the opinion that we have done that well. I would look at the recent Iranian negotiation, and I think we came out total losers on that. We could go back a generation to the South Korea negotiations. All of these are on nuclear weapons and we absolutely made North Korea—we made it possible for North Korea to be a nuclear power based on our negotiations. So I myself don't feel a sense of comfort.

I yield back, Mr. Chairman. Thank you.

Chairman LUETKEMEYER. The gentleman's time has expired.

We go to the gentleman from Texas, Mr. Green.

Mr. GREEN. Yes. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. Thank you.

Mr. GREEN. And I thank the witnesses for appearing as well. In this area of enhancing the oversight ability of Congress, is there

something that is typically expected when we are negotiating these international agreements in which Congress would be involved?

Yes, sir?

Mr. ZARING. In my experience, regulators benefit most when they have authorization from Congress. And in that sense, congressional involvement is essential at the beginning of the process. But while the negotiations are ongoing it seems to me that passing legislation that then requires burdensome administrative procedural requirements doesn't benefit our perspective in coming up with the best deal we can in an organized coordinated way by regulators who are charged with consulting with stakeholders and interested parties, like the clients of the other members of the organizations to which the other witnesses belong.

Mr. GREEN. Yes, sir?

Mr. THOMPSON. Congressman, if I could just respond to that, I guess the question we are struggling with is that FIO and the Fed are supposed to be representing the U.S. regulatory system at these international discussions, but they are supposed to be representing the U.S. regulatory system, U.S. policyholders, and U.S. companies. And without a consensus view or some type of due process such as what is put forth in this draft legislation, how can that important representation be achieved?

That is why we think that this draft discussion is a very important piece of consideration for the committee.

Mr. GREEN. Yes, sir?

Mr. TORTI. If I may? Thank you, Congressman. The point is for Congress to set out objectives and goals for regulators so that we can have a unified approach in these negotiations, and that will strengthen the U.S. position. The point is not to in any way tie the hands or put a layer of process that is unworkable on top of what we currently have through the Dodd-Frank Act. It is to end up with a unified approach and a strengthened position by the U.S. negotiators in these deliberations.

Mr. GREEN. Under FIO and Dodd-Frank, it appears that the negotiator, which would be the Director of FIO, is to consult with the State insurance regulators, is to coordinate Federal involvement and policymaking related to these matters. So we have a means by which we can do this under Dodd-Frank, but we are now going to add some additional requirements. Is that the way you see it?

Yes, sir?

Mr. ZARING. That is precisely the way I see it. FIO has been given the authority to negotiate and the requirement to consult and that seems to me to be a good thing and the right way to set up the priorities for the head of the organization.

Mr. GREEN. Yes, sir. And in giving your response, would you kindly address the question of, do you ever get to a point where you have too many people trying to do one thing, which seems to be what we have already given as an assignment, but now we seem to want to have additional input after having given the assignment. Yes?

Mr. THOMPSON. You are absolutely right. You could have too many people at the table. And certainly, we would agree that the Director of the Federal Insurance Office, as well as the Fed, should be representing U.S. interests. What we are suggesting is rep-

resenting what? Under what authority and guidelines are they negotiating on behalf of the U.S. insurance industry and the U.S. Government?

What this draft legislation would do would be simply to provide those guidelines, that framework which sets the boundaries on which they can and cannot negotiate. That is all we are asking, and that is why we are supportive of this draft discussion. It is not to get involved in the way but it is simply to set the guidelines so that we are all clear on what is negotiable and what is not negotiable.

Mr. GREEN. Thank you, Mr. Chairman. I yield back.

Chairman LUETKEMEYER. The gentleman yields back.

Mr. Posey, the gentleman from Florida, is recognized for 5 minutes.

Mr. POSEY. Thank you, Mr. Chairman, and thank you for holding this hearing. I also thank the witnesses for your input. It is very informative.

To the chagrin of some, I guess, I don't work for the United Nations, I don't work for the E.U., I don't work for any other government except for the United States of America, and I don't think that my constituents should be governed or regulated by any other governments either.

It seems like with every international agreement we make of any kind, we are left holding the bag. And oftentimes, as I think Congressman Pearce was alluding to in his discussion, there are predetermined outcomes already before we even start negotiating before or after the document is signed that are not beneficial to us.

We deal with other governments where it is considered ethical to lie if you can harm America. We are supposedly under the impression that you are not supposed to lie to anybody for any reason. So, I think that this would be another case where we will get the short end of the stick.

Mr. Torti, the United States has a very long-held and proven tradition of State-based regulation. It has worked for 150 years. And you have a distinguished career of public service as Rhode Island's Banking and Insurance Commissioner. We are all aware of that. And you were recognized as a national leader on insurance regulation, so I might ask you if you can explain to members of the committee how the State system of insurance has evolved? How it has adapted to remain effective over time and comment on the steps that have been taken to address the concerns that resulted from the financial crisis?

Mr. TORTI. Thank you, Congressman, and I will try to the best of my ability to do that. It would take a lot longer than the few minutes we have left, but I will concentrate on the one area that I think is important here. But I will clarify again that I no longer represent the regulators or the National Assessment of Insurance Commissioners. I am trying to—

Mr. POSEY. Yes, you are running out of time. Get to answering the question—

Mr. TORTI. Okay. I am trying to describe a process and I will. We have significantly strengthened as regulators, State regulators have significantly strengthened group solvency requirements. We do still have a legal entity-type of a regulatory process, however,

there are all kinds of new holding companies' requirements in place.

There is a Form F it is called in the Holding Company Statute. It is the model statute. That is required for accreditation. That requires an enterprise risk management report be filed with the regulator.

There is what is called an Own Risk and Solvency Assessment (ORSA), that asks the industry participants to disclose all of the risks that they are subject to enterprise-wide and not just legal entity.

There are supervisory colleges that we hold for internationally active insurance groups and other insurance groups where all of the regulators from the various countries that the companies are doing business in get together to discuss legal entity and group-wide risks that are being faced by those companies.

So there is much in place now to fill the perceived void that may have been out there prior that we did not look outside the legal entity to regulate insurance.

That is not the case. There has been a lot done over the last few years and even prior to that we had group solvency issues working groups, and we had groups to modernize insurance regulation that were looking at group issues. There is also a group capital calculation—

Mr. POSEY. Let me just interrupt a minute because we are—

Mr. TORTI. Sure.

Mr. POSEY. —about to run out of time. In Florida, our Insurance Commissioner, Kevin McCarty, has a long, strong history of watching out for the consumer first and foremost. He doesn't care if a State Senator gets in the way. He will run over him. He doesn't care if a State Representative doesn't like what he is doing. He will jam horns with the Governor if necessary.

He does what he thinks is in the best interests of Florida consumers period, end of subject. I assume you and other Commissioners in other States do the same. My concern is that a bunch of foreign agreement makers won't share that same loyalty to our consumers. Would you comment, either of you?

Mr. TORTI. I would be happy to. Yes, as an insurance commissioner I did have a loyalty to those consumers. That was my charge. That is what I did and I agree with you. It is possible that the interests of our policyholders, our consumers here in the United States won't be appropriately recognized in certain international negotiations or standard-setting procedures, I should say.

Thank you.

Mr. POSEY. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman's time has expired.

With that, we go to the gentlelady from California, the ranking member of the full Financial Services Committee, Ms. Waters, for 5 minutes.

Ms. WATERS. Thank you very much, Mr. Chairman. I would like to direct a couple of questions to Professor Zaring. We all remember the damage caused by the near collapse of insurance giant AIG. We all remember that for many reasons, regulators did not catch the riskiness of their activities. And of course, we all remember

that many of the provisions in Dodd-Frank were written with this very catastrophe in mind.

Now, we have draft Republican legislation before us that would force U.S. negotiators to forget all of that. The draft fails to list financial stability as a negotiating objective of the United States in setting international insurance standards. In fact, the draft specifically calls for negotiators to seek to achieve standards that reflect the State-based U.S. solvency regime. Do these limitations set us up to miss the next AIG?

And further, it seems that every day we hear a new story about the potential impacts of global headwinds on the U.S. economy. Market concerns in China, for example, have raised questions about the effect on the U.S. and the global economies, and yet it seems that the insurance industry is calling on our regulators to forget about global financial stability as it negotiates international standards. What are the risks to the U.S. and global economies if these calls are heeded?

Mr. ZARING. Thank you. It seems to me that one of the points of these international negotiations and the effort to create capital standards that work for companies both at home and abroad, is financial stability. That is the bottom line and critical focus of any sort of effort to create common international standards for internationally active insurance groups.

It is worth remembering that in the case of AIG, it was brought low by activity that happened in a foreign subsidiary, credit default swaps, but also by its securities lending practice. And that was something that State regulators could have overseen.

I think the calamitous collapse of AIG indicates that three things are critical for controlling the way that the international insurance system works if it is to work in a way that is going to avoid any financial crises in the future. First is that a group-wide perspective is critical for ensuring that financial stability happens, that all of the entities within an insurance conglomerate have to be supervised.

These days that increasingly necessarily requires an international perspective given that the kinds of companies that can threaten the financial system like AIG operate in so many different jurisdictions.

And third, I think it suggests that subsidiaries can slip through the cracks of regulators. In that case, OTS, State regulators, and of course foreign regulators failed to identify the weaknesses in AIG.

And then finally, I think it is critical to remember in light of the problem of the global headwinds that face the American economy that insurance companies are not just a critical source of protection for consumers, but also a critical source of funding for our financial markets. And I think that is one of the things that animates supervisors when they worry about the risk that a foreign insurance company that provides a great deal of funding to American financial firms might collapse if inadequately supervised.

That is the kind of supervision and worst-case scenario that I think has meant that Congress has appropriately and Federal regulators are increasingly worried about the stability of foreign firms as well as domestic ones.

Ms. WATERS. While our State-based system for regulating the insurance industry certainly has its benefits, there are also some drawbacks. For example, the ability of States to deviate from standard insurance accounting rules by requiring less capital or fewer reserves or allowing certain risk in non-liquid investments to be counted as capital assets can weaken financial protections for consumers.

Also, differences across the States make it difficult for other countries to judge the strength of the U.S. system. Do you think there is room for better coordination among States to address these issues while still preserving a State-based system and the benefits that it provides?

Mr. ZARING. I do think so. And I think that our rich tradition of State-based consumer protection can only be augmented by coordination. And if that coordination is facilitated by the Federal Insurance Office, then it is all the better and more likely to be effective.

Ms. WATERS. I yield back the balance of my time.

Chairman LUETKEMEYER. The gentlelady yields back.

The gentleman from Ohio, Mr. Stivers, is recognized for 5 minutes.

Mr. STIVERS. Thank you very much. My first question is for Mr. Torti. We just heard some questioning from the ranking member about the AIG failure. Was any of that based on regulated, State-regulated insurance business?

Mr. TORTI. No. The financial products division was regulated by a Federal regulator, the OTS, which was eliminated as a result of the Dodd-Frank bill that was out there. Mr. Zaring mentioned securities lending. There were issues with securities lending, but it is my understanding the AIG life insurance companies would have survived without Federal aid despite the securities lending issues.

Mr. STIVERS. So the Securities and Exchange Commission and the OTS were Federal regulators who failed with regard to the failure of AIG, correct, Mr. Torti?

Mr. TORTI. That is correct.

Mr. STIVERS. Thank you. I just think that is really important to bring up as State regulators were just maligned. Under McCarran-Ferguson, we have had an incredible history of effective and efficient State regulation in my opinion.

Mr. Torti, as I am talking to you, State regulators don't have group capital standards today, but they have been working on a group capital calculation. Do you know how that is going? You are just recently transitioning and can you give us an update of where that might stand?

Mr. TORTI. Again, I cannot speak for the NAIC or the regulators.

Mr. STIVERS. From what you know when you left—

Mr. TORTI. Okay.

Mr. STIVERS. —are they close? Is it coming? Just tell us what you know and—

Mr. TORTI. Absolutely. The NAIC has basically voted to take an approach, an aggregation approach, to aggregate our current risk-based capital standard, the States' current risk-based capital standard, to come up with a group capital standard. They have assigned it to a subcommittee of the C Committee, the Financial Condition, and—

Mr. STIVERS. When do you expect it to be done? Give me a round number, 2016? Early 2107?

Mr. TORTI. They hope to make lots of progress by year-end, but again, I can't speak for the regulators.

Mr. STIVERS. Let me ask you the next question. Given that we all just agreed that under McCarran-Ferguson the State regulators are the prudential regulators, shouldn't they have time to work on their group calculation? The one shortfall I see in this bill is it requires the Fed to finish its capital standard, but it does not require the State regulators to even finish their group capital calculation. Shouldn't that be added to this bill?

Mr. TORTI. I think that would be a worthwhile addition to this bill.

Mr. STIVERS. Thank you. Let me ask the whole panel some questions. Do you believe that the benefits to domestic companies and consumers of reciprocity under a covered agreement are worth negotiating a covered agreement? Raise your hand if you believe that.

I figured everybody. Okay. Everybody, and let me note for the record that everyone agreed we should pursue reciprocity if it is in the interest of American consumers, American domestic companies. Would you all agree that our State-based system is effective at protecting both consumers and the solvency of our insurance industry? Raise your hand if you believe that. Three of four.

Let me ask really quickly of Mr. Zaring, do you believe in the State-based regulation system? Yes or no? Or would you prefer a Federal system? That is really all—I don't want a long answer. I have a minute here.

Mr. ZARING. The State-based system does an excellent job of consumer protection.

Mr. STIVERS. Okay. Thank you.

Mr. ZARING. I worry about it for solvency.

Mr. STIVERS. Got it. Okay. So the next question for the panel is, do you think that it is reasonable to set forward a system or a process, an orderly process for any international agreement? Raise your hand, yes or no. Three of four again. Thank you.

And now, since Mr. Zaring already spoke about the fact that he thinks a cost-benefit analysis is overly burdensome, let me ask if anybody else—and raise your hand if you think any of these things are overly burdensome—are clear objectives overly burdensome? No one believes that.

Is a public comment period overly burdensome? Nobody believes that. Is a semiannual report overly burdensome? He believes the semiannual report is too much work, one person. Four, is studying the impact on consumers overly burdensome? One person believes we don't want to look at what consumers say. That would cause too much burden.

Is a report on transparency of the IAIS overly burdensome? One person believes that transparency apparently is overly burdensome. What about domestic capital rules being promulgated so we know what the domestic standard is before we move to international agreement? Who believes that is overly burdensome? This is getting pretty repetitive, one person.

And last and finally, who believes a 90-day period to have Congress look at this is overly burdensome? One person. Okay. So it's

pretty clear that most people believe this is not overly burdensome at all.

Thank you, Mr. Chairman. I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired. Oh, they have called votes, and as of January 1st, they have really restricted the amount of time that they will allow us to show up late, so as a result we have about 7 minutes to get there and we only have 3 minutes to play with here. So if we stop along the way to get a drink of water, we are in trouble.

But we ask for the indulgence of the panel as well as those Members in attendance today. We will be back in probably about an hour. Until then, we will call a recess of the subcommittee.

[recess]

Chairman LUETKEMEYER. We did our due duty today to again pass some hopefully worthwhile legislation. With that, we will reconvene the subcommittee and go to Mr. Ross, who is up next.

I recognize the gentleman from Florida for 5 minutes.

Mr. ROSS. Thank you, Mr. Chairman. I am reminded of, as a child, when there was a move afoot to create measurement standards, international standards in the United States, metric. And they attempted to do that on road signs and whatnot. That didn't last very long, and mainly because of the great deal of resistance to it because we believe our standard of measure is very good.

I also think our standard of insurance regulation is by far the best in the world. And therefore I also have concerns about our ability to negotiate and Congress' ability to retain what I believe to be its primary authority in whatever may transpire in the negotiations with the International Association of Insurance Supervisors.

Ms. Cobb, you mentioned in your opening statement that similar risk characteristics should be treated the same, and yet you also expounded a little bit upon variable annuities. Is there any explanation that has been given for the unequal treatment?

Ms. COBB. No, Congressman, there hasn't been. The explanation is just a statement that variable annuities are more risky—

Mr. ROSS. Right.

Ms. COBB. —than products in other countries where the guaranteed interest rate is, in this environment now, say, 3.5 percent. Those other countries say that their contracts don't fall into the NTNI bucket—"Our products are not risky and yours are."

Mr. ROSS. Right. And what is the basis for the annuity anyway? What is going to be the benchmark for the interest rate? Those are things that need to be discussed because right now if we are going to it use to pay them, we are at negative interest rates, or for that matter the European Central Bank.

Ms. COBB. Yes.

Mr. ROSS. Mr. Thompson, I understand that your company has a footprint in 30 States but nothing internationally. Can you describe how the impact of international standards might still impact your company and others like yours if it is adopted by the United States?

Mr. THOMPSON. Absolutely, sir. So as we all know, I think, and can appreciate, economies around the world operate very differently, and as I believe you were a former State legislator—

Mr. ROSS. Yes, sir.

Mr. THOMPSON. —and Chair of the insurance committee, you have a pretty good understanding of the State-based regulation here. Fundamentally, as one example, insurance regulation in this country is entity-based.

Mr. ROSS. Right.

Mr. THOMPSON. So the discussion of AIG came up earlier. The insurance companies were protected. There was a discussion to raid the assets of the insurance companies to keep AIG from requiring Government bailout. The current regulatory framework in this country prevented that. That is not the case in many other countries.

And so things that are currently being discussed, which is group capital standards being applied here, don't mesh well with the current State regulations. And that is just one example.

Mr. ROSS. And what concerns me in addition to that, and Mr. Torti, maybe you might be able to address this as a former rate maker, is the matters considered in promulgating a rate include, of course, liquidity, capital standards, things of that nature, but what is going to be at issue is the verification of the solvency and the capital.

And when the verification process is gone through by the commissioner, it would expose most likely some proprietary information. And that has been, and I think very well-preserved by our individual insurance commissioners, but could there not also be an adverse impact from an international standard that would now require not only the verification of the capital but also the increased vulnerability of disclosing proprietary information?

Mr. TORTI. That is certainly a possibility, depending on what the standard required, depending on what type of calculation was necessary, some proprietary information of an insurance company could be exposed.

Mr. ROSS. One thing that hasn't been discussed and I want to just really hit on, because I think it is important back home especially for those of my constituents who are dependent on their financial products including their insurance products, what would be the impact on the consumers of international standards? Let us say we were to adopt Solvency II. What impact would it have?

And whoever wants to take that can. Ms. Cobb? Mr. Torti?

Mr. TORTI. Okay. I will take a shot at it. It could increase costs to consumers here in the United States. Putting it into—

Mr. ROSS. Minimal cost. Just the transformation of accounting procedures, you may be going from a risk-based capital to who knows what? And if you have to—that is an administrative cost that these companies are going to have to bear. Where does it—do they absorb it? No. They are going to pass it on.

Mr. TORTI. It is passed on to the policyholders, exactly.

Mr. ROSS. And without a doubt, I guess in my opinion, is that any change is going to result in an increase in premium to our consumers as a result of the adoption of this. One last thing is just a comment. I laud the chairman for this bill. I think it is important that Congress continue to be in the driver's seat on this with instructive measures as we have done in this part of the bill. And I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired.

With that, we go to the gentleman from Kentucky, Mr. Barr, for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman. I would like to know from the witnesses what your views are in terms of congressional involvement in oversight here. Professor Zaring, I think, commented in his prepared testimony that he didn't view that as being constructive in terms of being an impediment in the negotiations, in the international negotiations, to have Congress in the middle of this.

So given that we have a draft legislation that would enhance congressional oversight of this process, we will start with you, Mr. Thompson. Can you comment on how having Congress involved might enhance the process?

Mr. THOMPSON. Absolutely. Thank you for the question. And I think that goes to the heart of this draft legislation. It isn't to impair or impede negotiations. It is to provide clarity to those negotiations and also to prevent potentially catastrophic global regulations being back door-imposed on companies like mine domestically here, which has been discussed throughout this entire hearing the State-based insurance system in this country has served it very well for over a century.

Mr. BARR. Before we go to the other witnesses, are you concerned that not having Congress involved may exclude input from the State regulators?

Mr. THOMPSON. Yes, sir. Many of these discussions are taking place behind closed doors already. Therefore, we are asking Congress to, again, set those guidelines, set those boundaries. Let our negotiators at the table know what they can negotiate and what they can't right up front.

Mr. BARR. Thank you.

Mr. Torti?

Mr. TORTI. Sure. Thank you, Congressman. This is in no way intended to impede U.S. involvement in creating international standards. It is really to ensure a unified approach and to strengthen our position in those international negotiations. And increasing transparency clearly stating the goals and objectives of Congress will help to strengthen our position in these negotiations. We are all in a unified approach. You don't have any disparate opinions coming from the Team USA, to which we have referred.

Mr. BARR. Ms. Cobb, in addition to maybe answering that question as well, could you elaborate on the consequences that international standards imposing higher capital charges on U.S. insurance products like variable annuities might have on the domestic economy and especially for those policyholders?

Ms. COBB. Certainly, Congressman. First of all, we do agree with the current concerns that have been expressed here today. The question before all of us is how to fix it. The NTNI problems—I am speaking now of the IAIS standard-setting—the G-SII methodology problems, we rely heavily on Team USA. I could do a long list of our concerns but we don't have time.

But the question is striking a right balance in this bill and in our approach so that Team USA, the full Team USA, certainly including our State prudential regulators, Treasury, and the Fed have

the ability to participate fully in the international discussions—that is critical, we think, to a solution that can benefit U.S. interests.

Mr. BARR. What would be the consequences of substantially higher capital charges?

Ms. COBB. Substantially higher capital charges for NTNI variable annuity products in this country could make that product difficult to obtain for consumers. The consequences to U.S. insurers who are trying to compete overseas of having to post additional capital in that country because of these international standards are also considerable.

Mr. BARR. And in the course of the standard-setting—the standard-setting that is going to happen, I have been an advocate for tailoring of regulations in the financial regulation area based on size and complexity and activity of banks so that community banks, for example, would be subject to less regulation than larger more systemically important institutions. Is a similar tailoring relevant and important in the insurance space as well?

Ms. COBB. It seems perfectly reasonable. Yes.

Mr. BARR. And so I think Congress does have an interest in monitoring the process to make sure that we do take into account a tailored approach and on the size, bearing sizes and complexities of these insurers. Does anybody have anything else to add to that? I think my time is running out.

Mr. THOMPSON. I think the time is out, but I would just say we have concerns about trying to do such tailoring. State regulators are not going to be inclined to have multiple tiers of regulatory oversight and our fear is that the once common standard would be applied to all companies that they regulate.

Mr. ZARING. I will just say that Congress should definitely be involved however it sees fit, but if it is going to require American regulators to come up with an approach and then engage in international negotiations, then it is not clear what there is anything to negotiate over or if the rest of the world won't come up with its own standards as it is done in accounting, much to the—

Mr. BARR. Thank you. I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired.

The gentleman from Pennsylvania, Mr. Rothfus, is recognized for 5 minutes.

Mr. ROTHFUS. Thank you, Mr. Chairman. And thank you, panel, for being here this afternoon. Mr. Torti, if I could ask you this question? When you were a State insurance regulator, the NAIC opposed the decision by the IAIS to exclude consumer groups and stakeholders from working group meetings. FIO voted against the NAIC. Do you believe transparency and accountably have been reduced as a result of this decision?

Mr. TORTI. Absolutely, Congressman. The stakeholders are no longer allowed in the working group meetings and are not present when the decisions are made regarding these standards. So it definitely has reduced transparency.

Mr. ROTHFUS. Would the United States' position have been stronger had our representatives been on the same page?

Mr. TORTI. Yes.

Mr. ROTHFUS. Someone suggested that it does not matter what international standards the United States agrees to if they are subject to consideration in the United States before implementation. Mr. Torti, do you have any concerns about that approach?

Mr. TORTI. I don't have any concerns. I believe we should have a unified approach. I believe that the United States shouldn't come to the table with several varying opinions. I believe that we can work together to come to a consensus with State regulators and that approach would be the best to strengthen the U.S. position in any of these negotiations.

Mr. ROTHFUS. Mr. Thompson, according to many expert observers, the U.S. insurance sector remained relatively stable during the recent financial crisis, particularly when compared with the banking and securities sectors. Do you share this perspective?

Mr. THOMPSON. Absolutely, sir.

Mr. ROTHFUS. Can you attribute the strong track record to the unique nature of the business or the quality of regulatory supervision? Or is it a combination of both? Can you qualify that?

Mr. THOMPSON. Yes. I would attribute it to very strong oversight by State regulators who are focused first and foremost on policyholder protection, as well as insurance company policy protection. And I think their track record speaks for itself over the last 150 years that they have been responsible for regulating the insurance industry in the United States.

Mr. ROTHFUS. Mr. Torti, you argue in your testimony that without more congressional guidance on their objectives and priorities, our U.S. and State representatives can have conflicting perspectives and priorities, again, similar issue. Why is it important for the U.S. representatives in international insurance regulatory discussions, including the Federal agencies and the NAIC, to be on the same page?

Mr. TORTI. Again, I think the point is to have a unified approach. If we appear dysfunctional, if we are sitting at the table representing the United States yet having differing approaches on where we want to go with an international standard. You know, Dodd-Frank has affirmed State regulation as the system that is acceptable in the United States.

And State regulators and our Federal representatives need to work together to come up with that unified approach to strengthen our position in the international arena. And I certainly think that varying opinions among the players in this arena would cause significant harm to us in our negotiations on these standards.

Mr. ROTHFUS. Okay. Can you speak to whether States undertook any noteworthy reforms to address concerns arising from the financial crisis?

Mr. TORTI. Yes. And again, I don't speak for the NAIC. I am sorry to be repetitive on this, but I just want to make clear I am no longer a regulator. However, there have been many group solvency changes that have been made. There have been numerous working groups at the NAIC that have enhanced solvency regulations to look at a more group-wide approach but still keep our legal entity approach so that we ensure that policyholders are protected.

However, there are Own Risk and Solvency Assessment model laws that are going to be a part of the accreditation requirements.

There are holding company modifications that were made which deal with enterprise risk management. There are requirements to hold supervisory colleges for internationally active insurance groups.

There have been multiple enhancements to our financial analysis procedures to ensure that we are looking at group-wide risks when we look at a company. So yes, there has been a lot done since the financial crisis, and even before the financial crisis to look at the risk of the entire group.

Mr. ROTHFUS. I thank the panel, and I yield back.

Chairman LUETKEMEYER. The gentleman yields back the rest of his time.

With that, we go to the gentleman from Wisconsin, Mr. Duffy.

Mr. DUFFY. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. You can start your 5 minutes.

Mr. DUFFY. I want to welcome the panel, and just go over here on the far side for a quick question. In theory, and in theory only, is a covered agreement going to have minimal to no impact on Federal regulation or on our State regulators? Is that a fair assessment, Mr. Thompson?

Mr. THOMPSON. It is my opinion that there is a very real opportunity that future covered agreements could actually pre-empt State regulation. And that is our concern, which is why we think it is the purview or should be the purview of Congress to provide oversight and direction to those to make sure they don't bring up the obviously very successful State regulation we have in this country.

Mr. DUFFY. With that, okay. But by itself, by itself the covered agreement—

Mr. THOMPSON. No, sir. Absolutely, there is a place for covered agreements. We are not opposed to covered agreements at all.

Mr. DUFFY. But—

Mr. THOMPSON. We want to make sure they don't bring up State regulations.

Mr. DUFFY. I am well aware of your position, but—

Mr. THOMPSON. Okay.

Mr. DUFFY. —I think in theory just a covered agreement does not impact by itself—

Mr. THOMPSON. No, sir.

Mr. DUFFY. —Federal or State regulators.

Mr. THOMPSON. No, sir.

Mr. DUFFY. I think in this institution, some of us might get concerned, because I don't think the original drafters of the Environmental Protection Agency might have foreseen that they could have stretched and pulled the EPA into the Clean Power Plant Rule that came out. And so we do get concerned about creeping rules and creeping regulations.

So does anybody have an objection if we by legislation guarantee that we are going to protect our State-based model? Is it in essence we are going to buy a little insurance, if you will, guaranteeing that you are not going to impact our State-based American model. Does anybody disagree with that theory?

Mr. ZARING. I will just briefly say that, again, to me the worrisome example is accounting standards and Generally Accepted Ac-

counting Principles (GAAP). So we decided in the United States we are going to do things the GAAP way and we didn't care what the rest of the world was going to do.

Mr. DUFFY. Do you disagree that we shouldn't protect it? If we in the legislature think that we should protect the State-based model that we shouldn't have insurance?

Mr. ZARING. Of course it wouldn't do that.

Mr. DUFFY. Insurance business says we are not going to—we are going to guarantee that we protect that model, the State-based model. Do you disagree with that?

Mr. ZARING. The legislature has the power to regulate as it likes, but now there is another competitor standard out there for GAAP, International IFRS, and it is—

Mr. DUFFY. So is it then your position that we negotiate a covered agreement and we adopt it herein with the Fed and that is going to eventually be imposed on our State-based system? Is that what you would like to see happen here? And is that what is going to happen here?

Mr. ZARING. My understanding and expectation is that the hope of a covered agreement is that we can get to a modus vivendi where our supervisors and European supervisors recognize the quality of the work that each other are doing. And so I—

Mr. DUFFY. You are avoiding my question. It is going to say that the intent is not to impose any new capital standards on our State-based system, right? Is that the intent? Does anybody disagree with that? Or if that is the intent let me know. You would agree with that, right, given—Ms. Cobb, you agree, right?

So there shouldn't be any disagreement with our position that we want insurance. We want a guarantee that what you say is actually going to happen. We want to go through the legislative process. You wouldn't disagree with that, would you?

Mr. ZARING. I think it is possible to get—if we are going to empower Federal regulators to do their best job negotiating with their foreign counterparts—

Mr. DUFFY. Listen, because I am not—

Mr. ZARING. —that too much oversight is—that too many people—

Mr. DUFFY. But I want to be clear, is your testimony then that through this international negotiation we want to have an impact on our State-based system and the capital that they are required to hold. Is that your position? Yes or no? I don't have much time.

Mr. ZARING. I am not sure I understood the question maybe, but—

Mr. DUFFY. Okay. But you do disagree that we should have insurance to protect our State-based model. And I want to move on. I think, Mr. Zaring, you indicated that hands would be tied if Congress set the parameters of this negotiation. Is that correct?

Mr. ZARING. No. Congress has already authorized these sorts of negotiations to take place, but then the question is what kind of parameters should Congress impose?

Mr. DUFFY. So you agree that we we could modify our parameters after the negotiation takes place we can actually approve or disapprove of an agreement?

Mr. ZARING. Congress certainly has that power.

Mr. DUFFY. And do you agree with us exercising that power?

Mr. ZARING. If the agreement comes back in a way that is unfavorable to American interests, then I don't see why it wouldn't.

Mr. DUFFY. It worked for TPA, didn't it? TPA worked pretty well. We went through a negotiation, set the parameters, voted on it, and sent our negotiators free. Why wouldn't it work with international negotiations on insurance standards?

Mr. ZARING. I feel like we already have the authorization necessary.

Mr. DUFFY. Does anyone—oh, can I ask just one quick question? Is anyone concerned about a creation of a two-tier insurance system?

Mr. Thompson?

Mr. THOMPSON. I'm very much concerned about that.

Mr. DUFFY. Anyone else? Ms. Cobb, are you concerned about that?

Ms. COBB. I am not sure what you mean.

Mr. DUFFY. Do you want to have our Federal globally active 50 insurance companies have one capital standard and there might be a different capital standard for small mutuals that do business in a State or a few States. Does that concern you?

Ms. COBB. It seems perfectly reasonable to me if I were a regulator that I would want to assess companies according to the nature, scale, and complexity of their risk.

Mr. DUFFY. So you would say that you don't have a concern. There could be two models. You are okay with a small State mutual having a different capital standard than a large internationally active SIFI?

Ms. COBB. I don't know the answer to that question.

Mr. DUFFY. Anybody else?

Mr. TORTI. I just think that is already the case. SIFIs are subject to regulation by the Federal Reserve so there is an additional layer of—

Mr. DUFFY. We got that in Dodd-Frank, didn't we?

Mr. TORTI. —protection there.

Mr. DUFFY. Yes, we got that in Dodd-Frank. So my concern is we want to remedy Dodd-Frank and say we will have everybody subject to the same capital standards, which will endanger our State-based system. And that is many of our concerns.

So with that, I appreciate the indulgence of the chairman, and I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired.

With that, we have a redirect from Ranking Member Cleaver.

Mr. CLEAVER. Oh, thank you. This is kind of related to what Mr. Duffy was saying, and it is just one quick question. What would it look like? How would you paint of picture of what would happen if the United States just decided that it was going to retreat from participation in international discussions on insurance standards? What do you think would happen if we just said henceforth forevermore we are out?

Mr. ZARING. My concern, Congressman, is that then international standards would get made and they would get made without our input. And increasingly, as our insurance companies tried to do business abroad, they would find that they had to comply with

those standards, and they might regret the fact that we didn't participate in the process.

Ms. COBB. I agree with that comment. And I would say moreover to the extent that our domestic insurers are required to post additional capital or whatever in order to comply with insurance capital standards that had been determined internationally without our input, we are diverting capital away from our insurers selling insurance in emerging and other markets and in effect not creating jobs here at home.

Mr. THOMPSON. Mr. Cleaver, it is not our suggestion that we walk away from the table. We live in a globally connected world. We all understand that. What we are suggesting is we have a very good regulatory system in this country. We don't want that to be negotiated away in the international arena.

We think we are regulators. We think our representatives need to be at that table and they need to be negotiating and bringing the best insurance regulatory that we have in the world as demonstrated in this country to the table. And all we are suggesting is Congress has a role to play in that to provide the direction and the guidance to that negotiating team in order to bring that very effective regulation to the global marketplace.

Mr. CLEAVER. Thank you.

Chairman LUETKEMEYER. Thank you.

I think that was very succinctly put, Mr. Thompson. Let me add—I just have some closing remarks here before we wind up.

I think we need to be in a position to be able to negotiate as well as pushback as well as initiate. We need to be able to promote as well as defend. And so for us to go over to the negotiations and play defense all the time is important, but to be on the offense to show the rest of the world why our system works and theirs maybe doesn't work as well as ours. Maybe they need to change their system instead of we change to their system.

So I think, Mr. Thompson, you made a comment during the course of this with regards to they need to focus on regulation, the regulatory side, the industry side and the policyholders' side when the FIO folks go over there and work on these issues and represent us.

And Mr. Torti, you made the comment that Congress needs to set goals or guidelines for the regulators as they go through the process. And I think that is what we are trying to do with this bill. I think all of you have agreed that Congress has a role to play. We need to be in the approval process.

And a number of you have mentioned that there are Federal regulators that already go through a comment period and sort of approve things. But my concern is that if you look at the role that the Administration has played, and the lack of them listening to what we say as legislators, as what you say as industry representatives and what the comments that come from the consumers are ignored by the Administration time after time, day after day, industry by industry, agency by agency, there is great concern.

And that is the reason for the bill today is to see once if there is a way for us to structure this so we can put guidelines in place, guardrails, if you want to call them that, that will not hinder but enhance and then allow Congress to be there to be able to approve

or disapprove those actions in a way that we can protect the industry we have here, the regulatory system we have here and the consumers.

At the end of the day we need to be more watchful for and it is interesting because in my discussions with Mr. Sullivan as well as Mr. McRaith, they like our oversight. They like what we are doing here. They like a bill like this because from their standpoint it gives them leverage when they go negotiate.

They like for us to be involved, because when they go over there and talk to the IAIS folks they can sit there and say, hey, you know, we can't approve that. We can't approve this. We are going to go back and make sure this will work. And as a result it gives them what leverage they need to actually negotiate in better terms. So I think it is important.

This bill isn't perfect. We are still in draft form, and we want to continue with all of you and all of the folks who are represented behind you. Mr. Thompson, I believe in your testimony you made the comment that getting policy right is more important than unanimity.

I hope you all remember that as we go through the process because I am sure there is not going to be unanimity on everything that we do here, but end of the day we want to get the policy right to make sure we protect the industry, our regulators and their ability to do their job, as well as our consumers. And we have a wide group of interests here from very, very, very large international companies to local county mutuals, if you will.

And so we have a lot of work to do. I would like to get something put together in the next couple of months. So continue to be engaged with us. Continue to work with us on this. We want to listen to your suggestions. And hopefully, Mr. Thompson's wise words of, get the policy right and don't worry about unanimity, will be able to be the words of the day.

With that, again, I thank all of you for being here today. You did a great job of representing your industries in this important issue that I think is something we need. We have a little hearing day and it doesn't amount to a whole lot, but it is a really, really big deal from the standpoint of it affects every single person in this country because every single person in this country practically has some sort of insurance product. And so it is important that you are here to represent all those folks.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, this hearing is adjourned.

[Whereupon, at 4:53 p.m., the hearing was adjourned.]

A P P E N D I X

February 25, 2016

STATEMENT

OF

THE AMERICAN COUNCIL OF LIFE INSURERS

BEFORE THE

HOUSE COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON HOUSING & INSURANCE

ON

"THE IMPACT OF INTERNATIONAL REGULATORY STANDARDS
ON THE COMPETITIVENESS OF U.S. INSURERS: PART II"

FEBRUARY 25, 2016

STATEMENT MADE BY

CAROLYN COBB, VICE PRESIDENT & CHIEF COUNSEL,
REINSURANCE & INTERNATIONAL POLICY

Chairman Luetkemeyer, Ranking Member Cleaver, and members of the Committee, I am pleased to present this statement expressing the views of the American Council of Life Insurers (ACLI) regarding international insurance standards. The ACLI is a Washington, D.C.-based trade association with approximately 300 member companies operating in the United States and abroad. ACLI advocates in federal, state, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing more than 90 percent of industry assets and premiums.

LIFE INSURERS ARE ESSENTIAL TO RETIREMENT SECURITY

In the United States and around the world, retirement security is an increasingly urgent problem. Populations are aging, the ratio of workers to retirees is declining, and governments are struggling to support the avalanche of retirees joining public retirement systems. Traditional pension plans that provide lifetime income are increasingly unavailable. Whether or not public programs will be able to continue to provide retirement benefits at current levels is an open question, and one that has dramatic consequences for the quality of life for millions of families. Financial security for families and dignity for all in retirement should be a goal of governments around the world.

The life insurance industry is uniquely suited to provide retirement solutions. Life insurers provide risk protection, insurance, and annuities products that help families save for retirement and ensure guaranteed income for life. Annuities are the sole means available in the marketplace today by which retirees can secure income for life. Now more than ever, life insurance companies are essential to helping families build and achieve retirement security. By strengthening retirement security, life insurers are improving the lives of retirees and also reducing demands on public programs.

LIFE INSURERS SUPPORT THE ECONOMY THROUGH LONG-TERM INVESTMENT

Life insurers are also important contributors to economic growth as long-term investors. Life insurers are leading purchasers of corporate bonds, which fund business expansion, innovation, job growth, and infrastructure. Because life insurers make guarantees that often last many decades, they must invest in assets that have the same long-term horizon. This kind of asset-liability duration matching is not only a fundamental principle of prudential regulation of insurers, but also positions life insurers to be a powerful source of long-term capital and economic growth. The bonds that life insurers purchase today have an average maturity of more than 18 years.

INTERNATIONAL CAPITAL STANDARDS SHOULD NOT PRECEDE DOMESTIC CAPITAL STANDARDS

Both the Federal Reserve Board (Board) and the International Association of Insurance Supervisors (IAIS) are developing insurance capital standards that are likely to have significant impacts on life insurance companies and the families who depend on them for financial and retirement security. If these standards are bank-centric or inconsistent, they will disrupt the marketplace and undermine the ability of life insurers to provide long term, guaranteed retirement products to savers and retirees. To ensure the best possible outcome for policyholders, the Board should utilize the flexibility provided in the Insurance Capital Standards Clarification Act, develop an insurance capital standard that is appropriate for U.S. insurers and the insurance business model, and partner with the other U.S. representatives to the IAIS (Treasury's Federal Insurance Office (FIO) and state insurance supervisors) to ensure that any international insurance standards reflect the unique strengths of the U.S. system of insurance supervision. As I will describe more fully later, U.S. insurance products are currently treated unfairly by the IAIS, which has approved a higher capital charge for U.S. variable annuity products but not for products offered in other countries with similar risk characteristics. U.S. insurance products must not be placed at a competitive disadvantage by international capital standards and all insurance products with similar risk characteristics should be treated equally regardless of their national jurisdictions.

The ACLI thanks Chairman Luetkemeyer, Ranking Member Cleaver, and the members of this committee for their support of the Insurance Capital Standards Clarification Act in the last Congress. As a result of the bipartisan leadership of this

committee, as well as bill authors Representative Gary Miller, Representative Carolyn McCarthy, Senator Susan Collins, Senator Sherrod Brown, and Senator Mike Johanns, both the House and Senate passed the Insurance Capital Standards Clarification Act by a unanimous vote, providing a clear statement that Congress supports appropriate capital standards for insurance companies. ACLI strongly supports utilization of the flexibility provided in that law and urges continued congressional oversight to ensure that the intent of Congress and the competitiveness of the U.S. insurance industry is preserved. ACLI commends the Board for its plan to conduct formal rulemaking with notice and public comment, and for its many public statements, including in testimony before this Committee, that it intends to exercise the discretion authorized by Congress to tailor capital standards to insurance companies. The Board's plan to tailor standards is very appropriate and will further the interests of prudential supervision of insurance companies.

It is essential that policymakers correctly address insurance capital standards here in the U.S. first, so that our Team U.S.A. representatives to the IAIS have a stronger, unified position in any international discussions. Common sense suggests that the U.S. should conduct its own process for the development of an insurance capital standard before agreeing to any international standards. The ACLI believes that it is in the best interests of the U.S. to focus on the domestic rulemaking first and ensure that the domestic process is as thoughtful, informed, and transparent as possible.

Any insurance capital standard must reflect the long-term nature of life insurers' investments and the need to match investments with the long-term duration of insurance liabilities. Bank standards that favor short-term assets simply do not work for the insurance company business model, in which commitments to insurance policyholders and annuity investors often last many decades. The ACLI believes that any consolidated capital standards developed by the Board for insurance companies should be modeled on the state insurance risk-based capital system. State risk-based capital standards are comprehensive standards specifically designed by insurance regulators to measure the unique risks of the insurance company business model.

U.S. LEADERSHIP AT FSB AND IAIS PROTECTS U.S. COMPETITIVENESS

The influence of the Financial Stability Board (FSB) and the development of capital standards by the IAIS, including the insurance capital standard (ICS) and Higher Loss Absorbency (HLA) requirements, represent a significant change in the development of standards for the insurance industry. The development of international insurance capital standards means that U.S. federal agency leadership by the Treasury Department and Federal Reserve Board, in partnership with state insurance regulators, is more important than ever before. The full involvement of Treasury and the Board in FSB and IAIS activities is absolutely essential to influencing the international process and ensuring that international standards reflect the unique strengths of the U.S. system for prudential insurance regulation.

Team U.S.A. representatives should work to ensure that any global capital standards do not disadvantage U.S. insurers and the families that rely on them for financial security. Any restriction on the ability of Team U.S.A. to participate in international standard setting organizations would in no way protect the U.S. insurance industry and U.S. insurance consumers.

COOPERATION AND COORDINATION OF TEAM U.S.A. APPROACH IS ESSENTIAL

ACLI commends the three U.S. insurance representatives to the IAIS (the Board, FIO, and state insurance supervisors) for the important partnership that they have established in the Team U.S.A. approach. Team U.S.A. will be best positioned to represent the U.S. and secure the best outcome for U.S. consumers and insurers only by working together, meeting regularly, coordinating their efforts, and agreeing to common objectives. The Team U.S.A. concept constitutes a cooperative effort to speak with a strong, unified voice as part of any IAIS discussions and ACLI fully agrees with the wisdom of this approach.

FSB AND IAIS PROCESS SHOULD REFLECT GREATER TRANSPARENCY AND ACCOUNTABILITY

The ACLI believes that both the FSB and the IAIS should work to improve their engagement with stakeholders and ensure that their governance procedures meet high standards. Ongoing engagement with stakeholders and transparent processes are critical to the development of thoughtful, informed policies. In the absence of

meaningful participation from public stakeholders, policymakers are denied access to a full exchange of ideas and a diversity of perspectives. In contrast, highly transparent processes and greater opportunities for stakeholder participation introduce more information, expertise, and experience to the discussion and increase public confidence in institutions.

IAIS bylaws and the IAIS Policy for Consultation of Stakeholders recognize the critical importance of open and transparent processes. ACLI appreciates this official commitment to transparency and accountability and urges the IAIS to redouble its efforts to make good on this promise. Due to the importance of the work being done by the IAIS, more stakeholder input is necessary, not less. With that in mind, we believe that the IAIS should take the following steps:

- Refrain from developing regulatory standards in isolation from the industry and the markets they serve.
- IAIS consultations should include a comment period of no less than 90 days to allow for thorough review and thoughtful comprehensive responses. For significant standards, 60 days is very often inadequate.
- To achieve the IAIS' stated goal of transparency, IAIS committee, task force and working group rosters must be posted to the IAIS Web site and updated regularly to reflect changes.
- IAIS meeting materials should be made available publicly and stakeholders should have access to agendas, presentations, detailed minutes, and advanced drafts of supervisory material.

COMMENTS ON G-SII ASSESSMENT METHODOLOGY

On January 25, 2016, ACLI provided comments to the IAIS in response to its public consultation on a proposed updated Assessment Methodology for Global Systemically Important Insurers (G-SIIs). ACLI welcomes the IAIS commitment to review and update the Methodology, which must be improved in significant ways. In order to meet the IAIS' goal of reducing systemic risk, the Methodology should focus on the creation and transmission of systemic risk. If not developed properly and fairly, the Methodology may diminish the availability of retirement security products at the expense of aging populations around the world.

We remain concerned that while the IAIS stated its intention to assess on a loss-given-default basis, the Methodology combines criteria that measure impact in the event of default with those that measure the vulnerability to market stress as measures of systemic risk. It also fails to recognize product and risk management techniques that reduce systemic exposures. In addition, the Methodology relies on a relative ranking of insurance firms to determine G-SII status. It is critical that assessment for potential systemic exposure be conducted through a loss-given-default lens and that vulnerabilities be demonstrated to link to a systemic risk transmission channel. It is equally critical that the assessment process be conducted in a transparent manner and include meaningful dialogue with the firm under consideration throughout the process so they understand the basis for their consideration and/or designation and measures that can be pursued to avoid or shed designation.

We would also underscore that there remains little empirical research and data to form the basis for an understanding of how activities insurers engage in could, in the event of disorderly failure, cause significant disruption to the global financial system and economic activity. We believe the IAIS and FSB should consider this threshold question and devote time and resources to improve this understanding.

COMMENTS ON APPROACH TO NON-TRADITIONAL NON-INSURANCE

On January 25, 2016 ACLI provided comments to the IAIS in response to its public consultation on Non-traditional Non-insurance (NTNI) Activities and Products. ACLI is very concerned that the IAIS approach to NTNI is misguided and troubled by the fact that it disproportionately harms guaranteed lifetime income products commonly available in the U.S. Specifically, variable annuities should not be considered NTNI and subject to higher capital charges. These products are strictly regulated by federal and state authorities and have helped consumers in America for 60 years. ACLI strongly believes that the NTNI approach must be fixed. That revision should better recognize the true nature of risk from an insurance balance sheet perspective and must result in a level playing field, particularly with products offered in other countries with similar risk characteristics.

Furthermore, ACLI believes that the IAIS consultation plainly misses its primary objective of considering systemic, macroprudential concerns. The NTNI approach emphasizes analysis of a company's probability of failure, which is a microprudential

concern, rather than analysis of how a company's failure might or might not impact the rest of the financial system, which is a macroprudential concern. ACLI supports reorienting the NTNI toward analysis of systemic factors.

ACLI is also concerned that the current NTNI definition excludes balance sheet risk management. The life insurance business model is to assume long-term risks and to implement proven strategies to manage those risks. Any framework that does not acknowledge and account for this critical element is incomplete and would be more likely to yield misleading results.

COMMENTS ON THE DISCUSSION DRAFT

ACLI would like to commend Chairman Luetkemeyer and other members of the Committee for their development of the Discussion Draft on international insurance standards. The Discussion Draft reflects many of the principles of transparency, accountability, and due process that are supported by ACLI and its member companies. The Discussion Draft improves Congressional oversight over international standard setting initiatives for insurance and expresses clear objectives for those initiatives, including maintaining the ability of the U.S. insurance industry to offer the products that U.S. consumers rely upon as part of their financial planning. These important goals are shared by ACLI and underscore the need for transparency and governance reforms at the IAIS and FSB.

ACLI would suggest some further refinements to the Discussion Draft for the consideration of this committee that are consistent with the view that any restriction

on the ability of Team U.S.A. to participate fully at international standard setting organizations would be harmful to U.S. interests.

We also have some concerns with the provisions of the Discussion Draft addressing covered agreements, which are not designed for enacting new international capital standards. Rather, they are a mechanism for removing commercial and regulatory barriers that may deny U.S. insurers full and fair access to particular foreign markets and for providing similar fair treatment to foreign insurers seeking access to the United States.

We appreciate that the 30-day public comment period proposed in the draft would run concurrently with the existing Congressional submission and layover requirement in the Dodd-Frank Act. However, we are concerned that the new requirements in the Discussion Draft could interfere with the effectiveness of covered agreements, including the currently pending covered agreement with the European Union, notice of which was published in the Federal Register last month. We pledge to work with the committee to address concerns while also preserving the effectiveness of this very important tool for helping U.S. companies receive fair treatment.

ACLI thanks the Committee for their leadership on this important legislation and looks forward to working with the Committee on suggested changes going forward.

CONCLUSION

Mr. Chairman, thank you for holding this hearing today to highlight the many concerns about international insurance standards. Any standards developed at international organizations must be consistent with the U.S. system for insurance supervision, must not disproportionately harm U.S. products approved and regulated by state insurance supervisors such as variable annuities, and must not interfere with the Board's rulemaking process, including notice and public comment, for development of insurance capital standards for insurers subject to Board supervision. Thank you for the opportunity to testify today and for your consideration of the views of ACLI and its member companies.

Statement

of

Gary Thompson

President/CEO

Columbia Mutual Insurance Company

on behalf

of the

National Association of Mutual Insurance Companies

to the

United States House of Representatives

Committee on Financial Services

Subcommittee on Housing and Insurance

Hearing on

The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers: Part II

February 25, 2016

Chairman Luetkemeyer, Ranking Member Cleaver and members of the Subcommittee, my name is Gary Thompson, and I am the President and Chief Executive Officer of Columbia Mutual Insurance Company. I also serve on the Board of Directors of the National Association of Mutual Insurance Companies (NAMIC) on whose behalf I am testifying today.

Columbia is a mid-sized insurance company based in Columbia, Missouri with direct written premium of over $262 million. For over 140 years, it's been our mission to build enduring relationships with customers by providing value and exceptional service in fulfilling our promises.

NAMIC is the largest property/casualty insurance trade association in the country, with more than 1,400 member companies representing 40 percent of the total market. NAMIC supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers.

NAMIC member companies serve more than 170 million policyholders and write nearly $225 billion in annual premiums. Our members account for 54 percent of homeowners, 43 percent of automobile, and 32 percent of the business insurance markets.

Through our advocacy programs we promote public policy solutions that benefit NAMIC member companies and the policyholders they serve and foster greater understanding and recognition of the unique alignment of interests between management and policyholders of mutual companies.

Both Columbia and NAMIC are very appreciative of this subcommittee's focus on international insurance issues over the past year and salute Chairman Luetkemeyer's efforts in crafting his discussion draft legislation. We have serious concerns about recent efforts to create international regulatory standards for insurance companies, and believe Congress should conduct strong oversight in this area in order to protect domestic insurance markets, companies, and especially policyholders. Strong legislation can help ensure this will happen.

Columbia is not an internationally active insurer, but our company, and companies like ours, are concerned about forcing uniformity across very different regulatory environments with very different economic and political goals. It is important to remember that the vast majority of US property/casualty insurers are not internationally active. In short, we worry about the potential negative impacts any international agreement could have on the domestic marketplace or the state-based regulatory system that has served consumer and insurer needs for more than a century.

International Regulation of Insurance

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 standards at home. It has also directly imposed its will on the policy development work of international standard-setting bodies, including the International Association of Insurance Supervisors (IAIS). The FSB is a group that is primarily made up of banking regulators. The members are not elected officials and they do not include any U.S. insurance regulators yet they seem to hold a great deal of global power.

The core role the IAIS has traditionally played is in crafting supervisory principles, standards, and guidance for its members, but especially to assist developing countries searching for a framework for insurance regulation. Prior to the financial crisis the IAIS focused mostly on its Insurance Core Principles, 26 broad themes for effective regulation. Historically, these principles were created as a resource for emerging markets developing regulatory structures, rather than a set of global rules. Following the financial crisis, the IAIS began to focus on global financial stability and producing an international framework for the supervision of large, complex, global insurance groups.

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 in crafting new regulations applicable to large global insurers. 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 identifying the problem the FSB was trying to solve, and without explaining why the decisions were made or why stakeholder comments were ignored. 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.

The specific direction in which the IAIS has moved presents other areas of concern:

- ***Legal Entity Regulation*** – The U.S. system of insurance regulation operates under the premise that a legal entity capital system is stronger and more protective of policyholders who rely on contractual commitments from the individual legal entity. The idea that group supervision and a capital requirement at the group level will create more sound regulatory protections ignores the impact on policyholders who rely on the legal entity from whom they decided to purchase insurance. Policyholders did not bargain for the transfer of group level contagion risk from one troubled legal entity within a group to a sound legal entity. While the legal contractual implications may vary between jurisdictions, this is a very important concept in the U.S. The recognition of the need for legal entity capital protection is critical and is something the IAIS seems to lack in its deliberations over the ICS. It should also be noted that this very system was tested in the Financial Crisis and performed well by any measure.

- ***Fungibility of capital*** – The movement away from the focus on supervision and capital requirements at the legal entity level raises questions about a supervisor requiring movement of capital between legal entities, also known as "'fungibility" of capital. This is of considerable concern for companies that operate with a business model based on legal entities. One need go no further than imagining what might have happened in the case of AIG if regulators or the securities subsidiary entities with all of the contagion risk had been allowed to simply raid the capital from healthy insurance subsidiaries to try and address the problem. Legal entity supervision obviates the need for fungible capital at the group level, a fact that supporters of an ICS seem to simply ignore.

- ***Accounting Standards*** – NAMIC has advocated for a flexible, principles-based approach that considers the regulatory outcomes of each jurisdiction. The IAIS seems to be committed to producing a prescriptive capital formula based on the same accounting information. They are creating a unique accounting system for insurance capital that bears more similarity to that used in the European Union. U.S. companies rely on Statutory Accounting for insurance regulatory purposes and publicly traded company use U.S. GAAP for investors. Changes in accounting standards would be very costly and very disruptive. If the U.S. supervisory, corporate law, and accounting systems are required to change significantly to accommodate the new group capital requirements, this will create a significant competitive disadvantage for U.S. insurers.

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 Role of Congress in International Discussions

At present, the U.S. is represented at the FSB by the Federal Reserve Bank's Board of Governors (Fed), the Securities and Exchange Commission (SEC), and the Treasury Department. The U.S. representatives to the IAIS include the Fed, the Federal Insurance Office (FIO), the National Association of Insurance Commissioners (NAIC), and all 56 state/territory jurisdictions. It is imperative that the various representatives that engage in these international fora speak with one voice in defense of the U.S. market, existing regulatory structure, insurers, and especially policyholders.

Congress has a critically important role to play in helping ensure the U.S. is appropriately represented in these international discussions. Through transparency and awareness, along with legislation to help guide our federal agencies, lawmakers can help protect the robustly competitive insurance market in this country. Rather than walk down the path of global regulatory uniformity for uniformity's sake, Congress can create an open process for deciding what is the best structure for the U.S. constituents of the insurance marketplace, including consumers, taxpayers, insurance companies, agents, and others.

In considering what course of action to take, it is important to remember that the various stakeholders in these discussions have disparate interests and objectives. There are some regulators in other countries who sincerely believe they have superior supervisory systems in place and that all other jurisdictions should adopt their approach. In our opinion, former SEC Commissioner Daniel Gallagher was correct when he said:

> It remains the height of regulatory hubris to assume that not only is there a single regulatory solution to any given problem facing our markets, but that a handful of mandarins working in an opaque international forum can find those perfect solutions. In reality, while such regulators may get some things right, they will most certainly get some things wrong — and, having coerced the world to do it all one way, it will go wrong everywhere.[1]

There are also going to be insurance companies which are domiciled or do business internationally that see a benefit to streamlining the regulatory requirements across jurisdictions. However, a benefit to some companies could be detrimental to others. For example, because the new standards being contemplated are more similar to existing European standards, U.S. insurers will be placed at a competitive disadvantage relative to their European counterparts who already must comply with them. At a Senate Banking Committee hearing last year, Dr. Adam Posen, the president of the

[1] Remarks at the Harvard Law School Symposium on Building the Financial System of the 21st Century: An Agenda for Europe and the United States, April 15, 2015. https://www.sec.gov/news/speech/building-the-financial-system-of-the-21st-century.html

Peterson Institute, suggested that insurers in Europe very much dislike their new regulatory system, Solvency II. However, because it seems inevitable, they have given up fighting it and instead back using international bodies to impose it on the U.S., Japan, and other global competitors.[2]

For domestic companies like mine, the chief concern is the eventual importation of foreign regulatory standards for all companies which supplant or duplicate existing standards that we know to be effective. Despite the fact that we do not do business internationally and the ICS would not apply to Columbia right away, we see this and other IAIS measures as a significant threat. The ICS is being developed with the intention of required global adoption. In the U.S., the implementation of the new standard would fall to the state insurance regulators. In the end, the idea that regulators would stop after only applying the standard to groups doing business internationally strains credulity. Inevitably, regulators will want all insurance groups using the same capital standards and at that point, it will apply to us.

We are urging Congress to weigh-in on this debate on the side of defending the existing state-based regulatory structure that we know to be time-tested and strong. The U.S. has the most competitive insurance market in the world and we must be careful to avoid undermining the existing regulatory system which fosters it.

The International Insurance Discussion Draft

Given the direction of many of the conversations at the IAIS, we believe that legislation from Congress is timely and appropriate. Since 2013, NAMIC has submitted comments and testified at the IAIS on numerous occasions to encourage IAIS members to listen to our 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" ICS standard, the IAIS is holding firm on many of the decisions it made in 2013.

It is clear to us that Congress needs to step in and clarify how it wants U.S. interests in international processes protected. For one, legislation must ensure that U.S. federal agencies engaged in international discussions regarding regulatory standards for insurance consult with Congress, state regulators, insurers, and consumers prior to, and during, negotiations. It must acknowledge that the outcomes of these international conversations are not binding on the U.S. and have no legal force unless enacted or promulgated by an insurer's state of domicile or its functional regulator. It must provide guardrails around what can and should be discussed through negotiating objectives and prohibitions for the federal agencies representing the U.S. at these negotiations. Ultimately, it must make clear that our existing state-based regulatory system is effective and must be defended and preserved. The U.S. regulatory system must be

[2]Testimony at Senate Banking Hearing on "The Role of the Financial Stability Board in the U.S. Regulatory Framework, July 8, 2015. http://www.banking.senate.gov/public/index.cfm/hearings?ID=A094AB96-17E2-47EF-B654-2CDA052BF765

recognized as the equal of every other country and any attempts to deem it otherwise should be dismissed out of hand.

The discussion draft legislation represents a good starting point for accomplishing these goals. We remain very appreciative of the work that Chairman Luetkemeyer and others have done thus far. We do however think that there are necessary improvements that need to be made to the bill before it is introduced. Additionally, we would not want to see the majority of the current provisions removed or weakened. Stakeholder unanimity is less important than ensuring that we get the policy right.

Below is a section-by-section outline of our specific comments on the bill text.

Section 2 - Findings
The findings section contains clear statements of Congress's views which we support on several important topics, including:

- The success of the state-based system of insurance regulation in the U.S. for 150 years
- The protection of policyholders has been the focus of regulation and ought to be the goal of any international standard-setting
- U.S. regulators ought to seek input from as many and as diverse a group of stakeholders as possible before representing the U.S. position abroad

It is imperative that the committee add another finding that makes it explicit that the international insurance regulatory standards at issue are not self-executing and are entirely without legal effect in the United States until implemented through the required federal or state legislative or regulatory process. The Fed may have the authority to impose certain supervisory requirements on insurers under its jurisdiction, however, neither the FIO nor the Fed have the authority to bind the U.S. state regulators or legislators to an international regulatory standard applicable to insurers not subject to Fed supervision. This point should be added to the findings in the bill.

Section 3 - Objectives for International Insurance Regulatory Standards
We believe Section 3 is one of the most important in the legislation. It should be clear to our federal representatives – and their negotiating counterparts – what is and is not on the table for negotiating. Providing negotiating objectives to be pursued helps focus the international discussions on the right issues while championing the U.S. system and protecting U.S. policyholders.

We support the included language to accomplish the following:

- Seek standards focused solely on the protection of policyholders as reflected in the U.S. solvency regime
- Promote a principles-based approach to insurance supervision, with a focus for capital adequacy on risk-based capital requirements
- Seek the most efficient and least disruptive way of assessing the capital adequacy of insurance groups

- Seek the recognition of the U.S. solvency regime as functionally equivalent to foreign regimes
- Seek increased transparency for all negotiations and meetings of international standard-setting bodies such as the IAIS
- Ensure sufficient public notice and comment periods before any standard is finalized
- Hold negotiating positions at international standard-setting bodies only after achieving consensus with state regulators
- Ensure the merits of existing state-based capital standards are recognized and incorporated in any domestic or global insurance capital standard

These represent excellent objectives for U.S. negotiators and should not be objectionable to anyone who believes the U.S. system is effective.

We strongly urge the committee to revisit putting in place several negotiating prohibitions as well. The right language would bar those things which should not be open for discussion while at the same time not tying the hands of U.S. negotiators to participate in and shape the international debates in the appropriate ways. For example, U.S. negotiators should be directed to oppose the application of bank-like capital standards for insurance companies or to oppose new standards which would require fundamental changes to how U.S. insurers are currently regulated. We believe this type of language is a necessary addition to any effective bill.

Section 4 – Requirements for Adoption of Int'l Insurance Regulatory Agreement
This section, also one of the more impactful, appropriately lays out further requirements before the U.S. may "agree to, accept, establish, or enter into" a finalized international insurance regulatory standard. It states that:

- The draft text of the new standard must be published in the Federal Register for public comment for a period of 90 days
- The Fed must issue a final rule for its own domestic capital standard and do so with notice and comment period of at least 60 days
- A copy of the final text must be submitted to the House Financial Services and Senate Banking Committees for a period of 90 days

The public comment and layover provisions of this bill will help to ensure that there is sufficient transparency with respect to the specifics of any agreement that is being considered, and we are very supportive of these. We are also very supportive of the sequencing provision that mandates that the Fed establish its required capital standards before negotiating internationally on others. There has long been a shared concern over the influence international negotiations might be having on the eventual domestic standard.

Roy Woodall, the Independent Member with Insurance Expertise of the Financial Stability Oversight Council (FSOC), perhaps said it best: "Congress is right to be concerned about these ongoing efforts by foreign organizations that could be used to

mandate changes in decisions that Congress has specifically left to our State regulators, or have been reserved for Congress itself to decide"[3] If the Fed has not yet decided what it believes the best consolidated group capital standard to be, from what position is it negotiating in these international arenas? The sequencing provision brings the Fed's focus back to the U.S. insurers and market, where it should be.

In the latest iteration of the discussion draft, a "limited effect" clause was added under subsection(c). The intent of this provision seems to be in line with our overarching recommendation that the legislation make clear that the framework being created under the bill does not explicitly or implicitly suggest that the U.S. representatives to the IAIS or elsewhere have any authority to legally bind the country to a new standard. While we appreciate the inclusion of this language, we believe it needs to be further strengthened. We urge the inclusion of language that states unequivocally that the authority to implement a new international standard in the U.S. resides solely with the functional state regulators or, in the case of Systemically Important Financial Institutions (SIFIs) or Savings and Loan Holding Companies, with the Fed.

Section 5 – Reports

NAMIC supports all efforts to maximize the transparency of international standard-setting bodies. The bill requires Treasury and the Fed to submit both a report and testimony every six months to the Senate Banking and House Financial Services Committees on efforts with state insurance regulators with respect to global regulatory forums. The report and testimony is to include:

- A description of the insurance regulatory or standard-setting issues under discussion at international bodies including the FSB and IAIS
- A description of the effects that proposals could have on consumer and insurance markets in the U.S.
- A description of any position taken by Treasury, the Fed, or FIO
- A description of efforts by the aforementioned to increase transparency at the FSB and IAIS
- A description of how the negotiating objectives in section 3 are being met and if they are not, why not

All of the above would be useful information for Congress to have and we support this type of consultation with both chambers. We would recommend a further subject upon which to report, namely, a description of any federal or state law or regulation which might have to be enacted or amended if any proposal being discussed at international insurance regulatory or supervisory forums were adopted. We would further recommend that the committee specify that Treasury and Fed study the effects of any proposals on "consumer cost and choice for insurance products" in the U.S.

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[3] Testimony of Roy Woodall, House Financial Services Subcommittee on Housing and Insurance Hearing on "The impact of Domestic Regulatory Standards on the U.S. Insurance Market," September 29, 2015. http://financialservices.house.gov/uploadedfiles/hhrg-114-ba04-wstate-rwoodall-20150929.pdf

Of particular importance in Section 5 is the inclusion of a joint economic impact analysis by the Fed and Treasury to be concluded prior to agreeing to any new regulatory standard. This study would be open to a notice and public comment period and most importantly, it would be independently reviewed by the Government Accountability Office. It is clear that both the FSB and IAIS tend to move forward on regulatory initiatives without a full assessment of the impact on U.S. consumers and insurance markets. This analysis and third-party review will help ensure that the impact of agreeing to some of these standards will be fully understood before they are finalized.

Section 7 – Treatment of Covered Agreements

The Dodd-Frank Act empowered Treasury through the FIO and the United States Trade Representative to negotiate and enter into international "covered agreements" on insurance regarding prudential measures. A covered agreement is wholly created by and defined in Dodd-Frank; a newly created term for insurance and not a standard type of contract, covenant, understanding or rule, subject to existing and recognized practices and requirements. These agreements are between the U.S. and one or more foreign governments or regulatory entities and must "achieve a level of protection for insurance or reinsurance consumers that is substantially equivalent to the level of protection achieved under State insurance or reinsurance regulation."

The scope of covered agreements is not well-defined, but they do have the power to preempt state insurance law if that law goes against the terms of the agreement. Exactly how these agreements will be negotiated, entered into, and applied are subject to general guidelines in Dodd-Frank, but questions remain concerning these agreements, their application, the rights of parties to participate in and/or challenge them, and the enforcement mechanism.

We remain very concerned about the mechanism of the covered agreement and believe they should be included under the guidelines and processes laid out in the bill. In previous iterations of the bill Section 7 did incorporate covered agreements under the scope of the bill, exempting the one currently being negotiated. We saw this as one of the more important provisions in the bill. Unfortunately, the latest version of the discussion draft moved covered agreements outside of its purview. With the authority to preempt state law built in, covered agreements are arguably more in need of monitoring, stakeholder input, and Congressional consultation and direction. We respectfully urge the committee to include covered agreements within the scope of the eventual bill.

Section 8 – Duties of Independent Member of Financial Stability Oversight Council

The FSOC – one of the more opaque extra-regulatory bodies currently in existence – remains a source of major concern for NAMIC members. We do however support the inclusion of the Independent Member with Insurance Expertise of the FSOC in international discussions regarding insurance regulation. The bill includes additional specific consultative authorities for this individual. In effect, it assures that the independent member will have the ability to:

- Engage in international dialogue on insurance regulation
- Work with the FIO and Fed at the IAIS and become a non-voting member thereof
- Participate in discussions related to insurance at the FSB and provide for attendance and participation of state insurance commissioners
- Participate with the U.S. delegation to the Organization for Economic Cooperation and Development

NAMIC members support adding more voices with insurance expertise to international discussions that are taking place. Given the role that the Independent Member with Insurance Expertise plays in the designation of SIFIs at the FSOC, this inclusion is more than warranted.

Of particular importance to the insurance industry is the provision allowing state insurance regulators to attend FSB meetings. We have long been critical of the FSB which has no insurance expertise from the U.S. and little expertise from other countries other than the IAIS representatives that report to them (there are no U.S. state insurance regulators or lawmakers represented on the FSB). Having additional, functional insurance regulators in the room can only help the FSB arrive at better decisions when it comes to insurers and insurance markets. We wholeheartedly endorse the inclusion of this provision.

Conclusion

It is clear that allowing U.S. officials to negotiate and engage with international regulatory bodies without Congressional input and direction would be a mistake. The development of the ICS points to many outstanding concerns including an over-reliance on uniformity, disregard for fundamentally different regulatory and legal systems, and a lack of true consideration of potential costs.

NAMIC and its members are pleased with the direction this legislation is heading, but believe there are ways in which it still needs to be strengthened to facilitate a needed course correction. In particular, we believe any effective legislation must:

- Clearly acknowledge that any international standard is not self-executing and is entirely without legal effect in the United States until implemented through a federal or state legislative or regulatory process.

- Add language that prohibits U.S. representatives from agreeing to standards which would require any additional changes to current state or federal law.

- Revisit the inclusion of covered agreements under the bill's processes and requirements.

By adopting these and the other recommendations listed above, the committee can help protect the robustly competitive insurance market in this country by swiftly moving forward on impactful legislation.

Property Casualty Insurers
Association of America

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TESTIMONY OF JOSEPH TORTI, III
VICE PRESIDENT OF REGULATORY AFFAIRS
FAIRFAX FINANCIAL HOLDINGS LIMITED
ON BEHALF OF THE PROPERTY CASUALTY INSURERS
ASSOCIATION OF AMERICA (PCIAA)

"The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers: Part II"

SUBCOMMITTEE ON HOUSING AND INSURANCE
COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

FEBRUARY 25, 2016

Chairman Luetkemeyer, Ranking Member Cleaver and members of the subcommittee, I commend you for holding this important second hearing on "The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers" and appreciate the opportunity to provide testimony. Fairfax Financial Holdings Limited ("Fairfax") is a global group of companies including insurers and reinsurers with significant operations based in the U.S. Our companies write "Main Street" commercial and personal property and liability insurance, as well as specialty insurance coverage including surety, long haul trucking, workers compensation and energy and agriculture related insurance. Fairfax's international operations include offices in Asia, Europe and the Middle East and includes Odyssey Re, a U.S.-based reinsurer that provides reinsurance for risks in over 100 countries.

My name is Joe Torti. I am the vice president of Regulatory Affairs for Fairfax, testifying on behalf of the Property and Casualty Insurers Association of America – PCI. Fairfax is a member of PCI, which is composed of nearly 1,000 member companies, representing the broadest cross section of insurers of any national trade association. PCI members write more than $195 billion in annual premium and 35% of the nation's home, auto and business insurance, with a membership epitomizing the diversity and strength of the U.S. and global insurance markets.

Until two months ago, I was the Rhode Island Superintendent of Banking and Insurance, so I can provide a broad perspective on the interplay of banking, insurance, regulators and the insurance industry.

PCI supports the Subcommittee's efforts to draft consensus bipartisan legislation clarifying its intent on insurance regulation and international representation and appreciates and supports the Chairman's ongoing leadership and evolving legislative drafts.

Congress in the Dodd-Frank Act affirmed the state-based regulation of insurance and the McCarran-Ferguson Act and the states' historic focus on consumer and policyholder protection. But there have been a number of emerging gray areas as the new regulatory roles have evolved where additional Congressional clarity could be very helpful. For example, Congress abolished the Office of Thrift Supervision and transferred its authorities over thrifts with insurance affiliates to the Federal Reserve Board. But the Federal Reserve has taken a dramatically different approach to its supervisory role than the OTS, including actively participating in the International Association of Insurance Supervisors (IAIS) together with the newly created Federal Insurance Office (FIO) and numerous state insurance regulators. The Dodd-Frank Act includes a brief reference to FIO's role at the IAIS, but provides no guidance as to how the Federal Reserve, FIO and states should work together, what their goals should be, and how they should defend the U.S. insurance regulatory system internationally.

I can tell you from personal experience as both a bank and insurance regulator that the two supervisory perspectives can be dramatically different, for example on issues such as capital leveraging and liquidity risk, or the more holistic issues of macro-economic stability versus policyholder protection. Congress recognized the need to address the regulatory divergence and provide more guidance with passage of the Insurance Capital Standards Clarification Act two years ago, clarifying that the Federal Reserve Board can apply insurance-based capital standards – rather than bank-centric rules – to the insurance activities of insurance holding companies it supervises. The Luetkemeyer draft legislation similarly clarifies the intent of Congress on international issues to follow a more insurance centric approach for insurance issues, including collaborating with the state insurance regulators and seeking greater equivalent recognition of the U.S. insurance regulatory system internationally.

Our state and federal representatives negotiating international insurance standards do their best to represent their agencies and ultimately the United States, but they have very different perspectives, constituencies and priority objectives. For example, in 2008 the Department of the Treasury in its Blueprint for a Modernized Financial Regulatory Structure recommended an optional federal charter. The Federal Reserve is in the process of creating a consolidated supervisory system for entities within its jurisdiction, essentially creating a second layer of holding company oversight. The states have generally opposed federal regulation of insurance except in limited instances. And yet all three with their very different regulatory perspectives and goals are in some manner representing the United States at the IAIS in the development of global insurance standards that could have profound implications for the future of our regulatory system.

Congressional oversight has been very helpful to the evolving U.S. process, particularly in encouraging regulatory cooperation and transparency. By working towards and considering bipartisan legislation Congress can help ensure that our Team USA regulators have the same priorities and objectives and greater Congressional clarity in carrying out their missions. This in turn will improve the likelihood of efficient and effective outcomes in international insurance regulatory deliberations that will serve consumers and maximize competition and innovation. PCI therefore appreciates the interest and leadership by members of the Subcommittee and full Committee towards that end.

The State-Based Insurance Regulatory System Has Been Successful Because It Is Consumer Focused.

For nearly 150 years, the states have regulated insurance and coordinated their activities through the National Association of Insurance Commissioners. As a former chief regulator from the State of Rhode Island and chair of one of the NAIC's most important committees, I know what effective regulation requires and how very well my state colleagues have performed in good times and bad, including during the financial crisis of 2008-2009.

While it has not always worked perfectly, the overall performance of the state-based regulatory system compares favorably with that of any other financial services regulation. In terms of size, degree of consumer protection, financial strength and amount and diversity of competition, the U.S. state-based insurance regulatory system is unmatched by any insurance regulatory system. We are pleased therefore that the draft legislation being considered by this committee begins its findings with a recitation of this fundamental reality.

This success is not just an accident or an historical anomaly. The U.S. insurance regulatory system has been so successful because it focuses on the end user—the consumer. So we strongly support Congressional emphasis on the importance of putting consumer protection first, as does our state-based regulatory system.

The U.S. Needs to Speak with One Voice in International Regulatory Discussions.

In recognition of the strong performance of state regulation, Dodd-Frank reiterated the primary role of the states in insurance regulation. However, it also created the Federal Insurance Office (FIO) in the Treasury, which under Title V is to coordinate federal policy and represent the Secretary of the Treasury, as appropriate, at the International Association of Insurance Supervisors. The FIO Director has since assumed a leadership role at the IAIS, chairing one of its two most important committees. In addition, Dodd-Frank gave the Federal Reserve Board regulatory authority over insurers with thrifts and those designated as systemically important. Based on this regulatory authority, it, too, is an active member of the IAIS. Meanwhile, the NAIC and states also serve on IAIS committees and the states have the largest amount of technical expertise in all areas and are legally responsible and accountable for the health and regulation of the markets in their states.

Unfortunately, without more Congressional guidance on their objectives and priorities, our U.S. and state representatives can have conflicting perspectives and priorities, for example taking three

different positions on whether to eliminate consumer group and stakeholder involvement in IAIS working groups. Both transparency and accountability have since suffered.

Accordingly, we support Congressional clarity to encourage greater collaboration and consensus among the regulators, requiring the regulators to work towards achieving consensus on policy positions in all international insurance regulatory discussions, backed up by reporting mandates. Congress often requires joint rulemakings or actions by agencies with overlapping jurisdiction. Federal agencies often fail to achieve such consensus within the statutorily required time, continue working on the issues in the meantime, and under Congressional pressure eventually get to the same page. While agreement among multiple agencies can be difficult, it is a critical effort to assure all representatives of the U.S. speak with one voice. It strengthens that voice and also increases the likelihood that any international standard will be effective and worthy of serious consideration. While there is no penalty in the bill that would tie the agencies' ability to take action to working together, Congress can and should set the appropriate goals and required eventual outcomes to ensure a cooperative approach.

Transparency and Accountability Are Often Lacking in International Regulatory Discussions.

As previously noted, the IAIS voted in 2014 to close its working group meetings, with a few rare exceptions, thereby reducing the ability of U.S. companies and consumers to participate meaningfully in the process. Every bit as important, the Financial Stability Board, which was given extremely broad powers by the G20 ministers to set the regulatory agenda for all financial services sectors including insurance, operates behind closed doors with an occasional invitation to selected companies. The Treasury, Fed and SEC are the sole representatives of the U.S. and the states are not present, even when insurance regulatory issues are considered.

Because transparency is a core value and is fundamental to our system, and because it produces the best over-all outcomes, it is critically important that Congress act to reverse the trend toward closing doors and excluding interested parties unless they have been blessed by the powers that be—often not U.S. regulators. The NAIC holds open meetings and conference calls of virtually all of its working groups and offers a good model of openness that has contributed substantially to the success of our system.

The draft legislation strongly encourages increased transparency, establishing greater transparency as a negotiating objective and providing specific procedures to assure transparency and accountability, for example public notice and comment periods in connection with the congressional layover provisions. The draft would also require special and periodic reports on transparency. While the specific requirements of the bill have been evolving, we support the efforts to provide greater clarity of Congressional expectations for increased transparency and accountability.

The other element of transparency that Congress should address is the current lack of information from federal agencies before, during and after international insurance regulatory deliberations at the IAIS, FSB and elsewhere. Congress makes the laws and has a unique role in protecting McCarran-Ferguson and setting the boundaries and limits for federal involvement in insurance.

Congress is kept regularly involved in international trade negotiations and the draft bill would appropriately require a measure of accountability to Congress for international standard setting negotiations as well.

The Need for Increased Mutual Recognition and Congressional Oversight of International Agreements

The EU, the second largest insurance market in the world, is now beginning implementation of Solvency II, a novel insurance regulatory approach based in part on global banking standards that reflect Europe's more concentrated and interconnected market, its tradition of greater intervention into the private sector, and the need for a more one-size-fits-all common market standard. Solvency II's approach and structure is fundamentally different from the time-tested state-based insurance regulatory system in the U.S. that is more focused on consumer protection and supported by extensive data reporting and guaranty funds in every state. It may be the right system for Europe, but has already proven enormously expensive with all of the Team USA representatives suggesting that portions such as required market valuation of liabilities would not be beneficial to U.S. consumers.

Unfortunately, Solvency II contains a requirement that companies from "third countries" including the U.S., be treated differently unless the third country is deemed to be equivalent, a highly prescriptive process. The U.S. understandably, and in consideration of the success of our different and time tested system, refused to submit to that process. Just before Solvency II implementation, UK regulators demanded extensive data reporting from U.S. companies, reaching beyond Europe to the U.S. holding companies, thereby impliedly giving extraterritorial effect to Solvency II. And it is not clear what steps other European regulators may take against our companies.

We are pleased that Treasury and USTR have indicated that they will push for recognition of U.S. regulation by the EU in connection with their discussions with the EU and do not intend to exceed their negotiating authority with respect to agreeing to domestic regulatory changes. While the draft legislation has been evolving in this area, we appreciate the Congressional vigilance and encouragement of the desired outcome.

Conclusion

Since the enactment of Dodd-Frank, the international insurance regulatory world has evolved in ways that may not reflect congressional intent to protect the strength and competitiveness of the U.S. insurance market and its consumer focused state-based regulatory system. We commend the Congress for its efforts to date and urge you to move forward with bipartisan legislation that includes the Luetkemeyer draft to improve international insurance regulatory deliberations and outcomes and clearly and effectively promote U.S. markets and our state-based insurance regulatory system.

TESTIMONY OF DAVID ZARING

Associate Professor of Legal Studies and Business Ethics, The Wharton School

to the

United States House of Representatives

Committee on Financial Services

Subcommittee on Housing and Insurance

Hearing on

The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers: Part II

February 25, 2016

I am an associate professor of legal studies and business ethics at the Wharton School. I study financial regulation and, in particular, international financial regulation, a field of growing importance and one that has already transformed the way that banks and capital markets are regulated. It is a field of increasing importance to insurance as well.

1. Overview

In my testimony today on international cooperation on insurance standards, I would like to focus on three points.

The first is that international financial regulatory standards protect American consumers and American financial stability in two ways. International standards create a level playing field for financial market participants when they expand their businesses abroad and can also prevent

disruptive financial contagion that starts elsewhere from affecting the American marketplace. Until recently, international insurance regulation was a relatively quiet field. But in the wake of the financial crisis, that has changed, and we should generally welcome the new vibrancy in institutions like the Financial Stability Board and the International Association of Insurance Supervisors in creating consistent capital standards and supervisory approaches for insurance companies, many of whom do business at home and abroad.

Second, it is important to remember that the United States has traditionally played a very strong role in formulating standards in matters of international regulatory cooperation, a role that would be threatened by legislation that ties the hand of its representatives. American regulators have substantially increased the degree of transparency of the international efforts to develop common capital standards for banks. They have also had a very large say in the sort of capital standards chosen. And they have set the terms of regulatory cooperation by capital markets overseers. It could hardly be otherwise given the size and strength of the American economy. On the other hand, where American regulators have not fully engaged in an international process, they may find themselves in a position where they must later accept standards that have been designed without their input – as the Securities and Exchange Commission has come perilously close to finding with regard to the development of international accounting standards. It is all but assured that representatives who represent everyone engaged with the domestic insurance industry would play a critical role in international insurance regulation given the size, strength and importance of the American insurance market. But if their ability to negotiate is curtailed, or if there are too many voices at the table, then their influence will likely be as well.

Third, while the importance of a transparent and open administrative process is undoubtedly significant, the best sort of transparency and democratic accountability is provided

by legislative authorization to engage in international negotiation at the beginning of the process, followed by domestic implementation through regular administrative procedure at the end of it. No global terms will be imposed upon American insurers until American regulators adopt capital or other rules through notice and comment, on a state by state basis, subject to state administrative law. In the past, American regulators have tailored international standards to meet the needs of the American market. In my view, it is important to remember that nothing binds American consumers or market participants until American regulators come home and go through the traditional role-making process with notice and comment. Attempting to add a new set of procedural obligations on top of this to the middle of the process that begins with congressional authorization and ends with domestic notice and common rule-making would be likely both burdensome and counterproductive.

2. The Progress of International Insurance Regulatory Standards

Insurance companies were thought to be relatively safe financial intermediaries. They were regulated, especially in the United States, more to ensure that they did not deceive consumers, rather than for the risk that they would collapse and create risks for the financial system. That perspective made sense, in most contexts; insurance companies are less susceptible to bank runs or the sort of fraud-based collapses that may roil the financial and capital markets. State insurance commissioners, who are close to insurance commissioners, have traditionally led the way in this oversight.

However, the financial crisis exemplified the ways that, as insurance companies have taken on more varied responsibilities, the largest of them can threaten the stability of the system.

Most notably, this occurred in the case of the insurance giant American International Group, one of the largest companies in the country. As you all know, it collapsed in 2008. AIG provided all sorts of insurance to policyholders all over the world. But its diverse array of products proved to be its undoing; AIG was ruined by its London subsidiary, AIG Financial Products. AIG-FP wrote insufficiently hedged credit default swaps, bolstered the strong balance sheet of the larger insurance firm. As the credit crisis worsened, AIG has to post more and more collateral to satisfy its counterparties that it would make good on the credit insurance it had written. Eventually the need to post ever more collateral rendered the company insolvent. To make matters worse, AIG's securities lending business collapsed at the same time. The result was that a famously careful American insurer that served different customers across the world was undone by one relatively small London subsidiary, who, it turned out, was not being carefully overseen by British insurance regulators, the New York insurance commissioners responsible for the rest of AIG, or the Office of Thrift Supervision, which oversaw AIG to the extent that the conglomerate served as a holding company of a thrift subsidiary.

The AIG experience, and the financial crisis in general, changed the way that oversight over non-bank financial companies was allocated between the states and the federal government, particularly with regard to the effort to create international standards. Title 5 of the Dodd-Frank Wall Street Reform Act created the Federal Insurance Office within the Department of Treasury. That office has limited powers, but has been given the responsibility to "coordinate federal efforts and develop federal policy on potential aspects of international insurance matters, including representing the United States" in the International Association of Insurance Supervisors (IAIS). The FSOC accordingly has three members focused on insurance matters: the

head of the FIO and a state insurance commissioner, neither of whom vote, and an independent member "having insurance expertise" who can vote.

IAIS began as a nonprofit corporation incorporated in Illinois. It was founded in 1994, in part at the urging of the Basel Committee on Banking Supervision, which began two decades earlier, and developed the first set of international capital adequacy standards for banks. The hope was that IAIS could do for insurance companies, who had become as global as any financial institution, what the Basel Committee did for banks.

IAIS's first two general meetings were held in conjunction with the annual meeting of the United States' National Association of Insurance Commissioners (NAIC). IAIS held its first annual meeting outside of the United States in 1996, in Paris. At first, IAIS represented insurance supervisory authorities in less than one hundred jurisdictions; however, by this decade, it had grown to encompass over 200 jurisdictions in about 140 countries, a base that represents at least ninety-seven percent of global insurance premiums. Since its creation, IAIS has issued global principles of insurance regulation, conducted research on supervision problems, provided training and support on issues related to insurance supervision, and organized meetings for insurance supervisors, including an Annual Conference designed "[t]o further encourage multilateral discussions on topical issues for insurance supervisors and other insurance professionals." (*About the IAIS*, INT'L ASS'N OF INS. SUPERVISORS, http://www.iaisweb.org/index.cfm?pageID=28)

In the wake of the financial crisis, IAIS, and the coordinator of financial oversight, the Financial Stability Board, under instruction from the G20, has taken new steps to create consistent global standards for supervisors designed to improve the safety and soundness of financial regulators. I will not go into these efforts in detail, but:

- The IAIS is developing capital standards for international active insurance groups. Those standards will consist of the sum of a basis capital requirement and a higher loss absorbency requirement. IAIS issued requirements on this score in October 2015.
- These capital requirements are part of ComFrame, a set of international supervisory requirement for the group-wide supervision of internationally active insurance groups.
- There has also been an effort to conclude a so-called covered agreement with the European Union. Concluding covered agreements are one of the FIO's functions,; they ae defined in Dodd-Frank as "a written bilateral or multilateral agreement regarding prudential measures with respect to the business of insurance or reinsurance that is (A) entered into between the United States and one or more foreign governments, or regulatory entities; and (B) relates to the recognition of prudential measures with respect to the business of insurance or reinsurance that achieves a level of protection for insurance or reinsurance commissioners that is substantially equivalent to the level of protection achieved under state insurance or reinsurance regulation." These agreements are meant to strengthen insurance regulation and level the playing field between for example the United Stated and European Union.

Efforts to create international insurance standards make sense as American firms increasingly enter foreign markets, and foreign firms enter the American one. Common standards level the playing field, and invite the sort of competition that can only benefit

insurance consumers. And in a world where an insurance group can be destabilized by a faltering subsidiary in a single country, the value of coordinated supervision is obvious.

Nonetheless, international processes are almost by definition more difficult to follow than domestic ones. IAIS and the FSB have taken, often at the behest of American regulators, steps towards improving their transparency. They have websites, they issue consultative documents and accept comment upon them, and they hold increasingly open annual meetings. And the IAIS has usefully dropped the very high fee it required of those who hoped to attend its annual meeting. But transparency should not be viewed as requiring that any and every interested party be able to attend any meeting at any moment. No business works that way, and nor does any agency. Policymaking requires opportunities for deliberation, and the importance of a role for deliberation should not be gainsaid.

3. Finding the Right Level of Transparency for International Insurance Standards

How can we ensure that these sort of international processes have the right amount of accountability and democratic legitimacy? At best, Congress will begin the process by authorizing, or in some cases blessing, efforts at international regulatory cooperation. Second, the regulators will engage in that cooperation. And finally, regulators must come home to enact rules, following the requirements of domestic administrative procedure that would apply to internationally active insurance groups.

So far, this is the process that has been followed in the recent international insurance standards. Congress authorized American participation in Dodd-Frank. Work on the standards is now ongoing. And American regulators participating in the process have repeatedly

announced that they look forward to underdoing the serious process of notice and comment here before any requirements are imposed on the American insurance market. These representations have been made before this committee, in fact.

Transparency is not helped, and substantial burdens are imposed by, imposing too many procedural requirements on the deliberation and negotiation process itself. Much of what goes on at institutions like the IAIS is a negotiation, and American representatives must have the ability to participate. That in turn means that public observer access for stakeholders to working groups and committee meetings do not make much sense. They limit the ability of negotiators to in fact negotiate – it risks creating the problems for international regulators that the well-intentioned Government in the Sunshine Act has created for domestic regulators such as the Securities and Exchange Commission, whose commissioners cannot meet privately to hash out their differences.

By the same token, requirements that proposed final agreements among international insurance regulators be published in the Federal Register is a needless layering on of notice and comment on top of notice and comment. Domestic regulators must and do bring international agreements back home for notice and comment before implementing them. And we have seen plenty of examples of cases where domestic notice and comment regularly changes the content of international agreements – the Fed's two-track implementation of the second version of the Basel capital accords is an example.

There is a little point in opening these agreements to notice and comment twice. By the same token, regular reporting on the progress of negotiations in public by the Secretary of the Treasury and the Chair of the Federal Reserve would be burdensome, only doubtfully illuminating and might make it difficult for the United States to adequately pursue its regulatory

interests in these international negotiations. I teach in a business school, and I rarely see my colleagues who teach our students to negotiate advise them to regularly make public disclosures of their goals and how they think the negotiations are going.

By the same token, covered agreements are meant to strengthen insurance regulation and level the playing field between, for example, the United Stated and European Union. Requiring them to be published before they enter into force in the Federal Register simply slows the process of implementing these agreements. It also suggests that the United States might not be able to live up to its bargains, which makes these agreements – which were blessed by Congress in Dodd-Frank – all the more difficult to conclude.

Finally, legislation that would require Treasury, the Fed and the state insurance commissioners to complete an analysis of the impact on consumers and markets of any international insurance regulatory standard and open that process to notice both before drafting the report and after the draft is completed would be extremely burdensome, especially compared to the value of such a report. I am unfamiliar with other similar requirements elsewhere in administrative law. Of course the report on the impact would not be binding in any way on the agencies that draft it, even if it cast some doubt on the value of the impact of international standards.

Finally, adding to the responsibilities of the independent member needlessly adds difficulties into the negotiated relationship for insurance regulators who already have enough problems coordinating the interests of the various agencies interested in insurance regulation including the fed and the treasury department. The federal government already has two representatives at IAIS, and the state insurance commissioners, of course, have always been involved in that organization. Adding a third federal representative to the group looks

superfluous, and makes the coordination process all the more difficult. It could confuse the other members of IAIS and undermine our ability to influence the process. As for the proposal that any state insurance commissioner be permitted to attend FSOC meetings when interested, it is difficult to see how that adds value, given that a state insurance commissioner already attends meetings of the council as a non-voting member. If every state commissioner attended, they would vastly outnumber everyone else in the room.

4. The Risks Of Non-Participation: The International Accounting Standards Saga

In my testimony, I have emphasized that international regulatory cooperation provides opportunities for American regulators to improve the stability of the financial system at home, and abroad, and therefore better meet their domestic regulatory mandates. I'd like to conclude with a cautionary tale about what can happen if American regulators ignore an international process, or approach it in a disorganized fashion.

The accounting story is particularly instructive. It is a cautionary tale for Americans because American regulators, by abandoning an already ongoing harmonization effort in the 1990s, lost their ability to affect the effort, and now have had to begin the process of conforming to it.

International accounting standards--the idea that companies listed on stock exchanges from Stockholm to Shanghai might report their results in the same way--have always been an attractive regulatory goal. In the 1980s, capital market regulators agreed to endorse an effort by professional accounting organizations to try for global harmonization of accounting rules. But

the effort proved controversial, as American regulators comfortable with the unique American approach to financial statements withdrew their support for the enterprise in the early 1990s.

That exit, however, did not stop the process of devising common accounting standards. Instead, the international efforts moved to Europe; the creation of international accounting standards after the SEC's rejection of the prospect of them, has been managed by the International Accounting Standards Board (IASB), a public-private arrangement based in London created in 2001. The IASB has devised a set of accounting standards, the International Financial Reporting Standards (IFRS), which has enjoyed quick adoption in European and other countries. IFRS was essentially created without American participation.

And therefore, perhaps unsurprisingly, IFRS is rather different from American accounting rules. It is a principles--rather than rules--based accounting system, in that it is less technical than traditional American accounting, and relies more on the gestalt of a company's returns to assess its accuracy. The United States had--and, for the moment, still has--a unique rules-based and reputedly challenging set of accounting standards that differ greatly from those of any other nation, the Generally Accepted Accounting Principles (GAAP).

But, faced with a cascade of adoptions of IFRS, those GAAP principles have a very tenuous future, despite the SEC's doubling down on their necessity in the 1990s. As foreign jurisdictions have gained more and more of the business of floating stocks and bonds and raising capital, American capital market regulators have given up hope that they might do so in ways consistent with the complicated GAAP. The SEC has permitted foreign companies that list on American stock markets to use IFRS to file their American annual and quarterly reports. And the SEC will surely accede to IFRS eventually for all filers.

Accounting is technical, and acronyms like GAAP and IFRS daunt almost as much as they reveal what, exactly, the distinction between rules-based and principles-based accounting really amounts to. But the import of the triumph of IFRS can be gleaned by abstracting away from it, and from the details of accounting. The commitment to an international effort in accounting has worked a sea change in the way that companies report their results, and the sea change has come without much American involvement--even though it will, in the near future, affect American companies as much as anyone else.

Thus, this story of accounting standards illustrates what those who worry what happens when regulators meet in a room have always suspected. Regulatory cooperation is easy to institutionalize--even when it crosses borders. Its propensity towards momentum is not a universal law, to be sure, but regulators ignore cross-border efforts at their peril, because those efforts can set the standards for even the most independent and recalcitrant jurisdictions, if the circumstances are right.

Thank you.

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February 25, 2016

The Honorable Blaine Luetkemeyer, Chairman
Subcommittee on Housing and Insurance
House Financial Services Committee
U.S. House of Representatives
Washington, DC 20515

The Honorable Emmanuel Cleaver, Ranking Member
Subcommittee on Housing and Insurance
House Financial Services Cmmittee
U.S. House of Representatives
Washington, DC 20515

VIA Electronic Mail

RE: Hearing entitled "The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers: Part II"

Dear Chairman Luetkemeyer and Ranking Member Cleaver:

The American Insurance Association (AIA) writes to express our appreciation for holding the hearing entitled "The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers: Part II." AIA represents approximately 325 major U.S. insurance companies that provide all lines of property-casualty insurance to U.S. consumers and businesses. AIA members write more than $127 billion annually in U.S. property-casualty premiums. Given the changing landscape in the global economy, it is crucial that policymakers continue to focus on competitiveness issues that affect U.S. insurers doing business in the international marketplace.

It is our hope that the subcommittee will recognize that the capacity to insure and spread risk, along with the capital required to do so, is increasingly affected by the international regulatory environment. The reality is that the major barriers to U.S. insurers in the rest of the world are largely regulatory. Now that Solvency II in the EU, and parallel regulatory regimes elsewhere, are coming into effect and being implemented, it is becoming clear that U.S. insurance groups with operations outside of the United States could face significant burdens if issues surrounding mutual recognition are not addressed. Therefore, it is imperative that international negotiations on how best to address these issues continue and that U.S. negotiators are supported to ensure that regulatory changes do not result in conditions that discriminate against U.S. insurers and reinsurers.

We are pleased that the subcommittee will also be discussing draft legislation that enhances Congress's oversight of international deliberations relating to insurance standards. We appreciate all the work that has gone into the draft language and believe that it contemplates several key issues.

AIA supports accountability and transparency, in both domestic and international standard-setting fora, and has consistently advocated for a united U.S. voice on international insurance issues. The draft legislation takes several meaningful steps to help ensure continued cooperation by U.S. representatives at international insurance standard-setting bodies, and improve transparency and accountability with regard to those ongoing processes.

Also, we appreciate the draft legislation's recognition of covered agreements as separate from other international negotiations. Covered agreements are important opportunities where the strengths of our system and the interoperability with other systems can be affirmed.

However, while we support many of the individual concepts in the draft legislation, we still have interest in and concern about the ultimate impact additional requirements on negotiators will have on the results in specific negotiations. Providing support and sufficient flexibility to U.S. negotiators, while preserving transparency and accountability, are essential requirements to realizing optimal outcomes for U.S. insurers and reinsurers. We look forward to further discussion at the hearing and will continue to evaluate the proposal going forward.

Finally, AIA appreciates that this legislation is not intended to address free trade agreements such as the Trans-Pacific Partnership (TPP), the Trade in Services Agreement (TiSA), the Transatlantic Trade and Investment Partnership (TTIP), and future trade agreements that are not yet contemplated. Trade agreements are subject to a high level of scrutiny and congressional engagement through trade promotion authority (TPA), and additional requirements are not necessary. AIA would request the subcommittee to consider explicitly excluding such negotiations and agreements from this legislation.

Negotiations and agreements can provide clarity and reduce the regulatory burden on U.S. insurers competing internationally. So, we again appreciate the subcommittee holding today's hearing and look forward to working to promote an international insurance marketplace that supports the U.S. state-based system and allows U.S. insurers to compete outside the U.S. on a level playing field.

Respectfully submitted,

Wes McClelland

Vice President, Federal Affairs
American Insurance Association

Congressman Roger Williams
Subcommittee on Housing and Insurance
"The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers, Part II"
February 25th, 2016

Statement and Questions:

Thank you Chairman Luetkemeyer and thank you to all the witnesses for your testimony.

Mr. Torti- in your testimony today, you stated that "for nearly 150 years, the states have regulated insurance and coordinated their activities through the National Association of Insurance Commissioners." You went on to say "while it has not always worked perfectly, the overall performance of the state-based regulatory system compares favorably with that of any other financial services regulation" and "the U.S. insurance regulatory system has been so successful because it focuses on the end user- the consumer."

While I support Chairman Luetkemeyer's efforts to make sure that U.S. Insurers have a seat at the table and establish some additional oversite, I'm concerned that these new international standards will hurt overall competitiveness. At the end of the day, as you said, I want to "protect the consumer" and make sure whatever model is established, if it is indeed inevitable, be in the best interest of American insurance companies. Although again- I'm not sure we need a new model.

Mr. Thompson, in a story I read this morning, I believe one of your senior VPs at NAMIC stated that if you want to change the law, "you shouldn't have to go to Europe; you should change it here"... As I've said, we have state legislatures that tweak these laws all the time and I think we need to continue to look at that as our starting point. Because as I see it now, the international capital standard setting process is moving ahead of U.S. rule-making process...

So let me start with Mr. Torti- Do you believe that the Federal Reserve should rely on state-based capital standards, and if so, do you feel it is important that state-regulators be engaged before these standards are developed?

Mr. Thompson – If I could add some thoughts on this issue, I would argue that it is essential that state regulators not only be engaged, but that they are relied upon in crafting the U.S. position for these international standard-setting discussions. With all due respect to the Federal Insurance Office and the Federal Reserve, neither one is an insurance regulator. The FIO has no regulatory authority whatsoever, and while the Fed likes to claim it "regulates 30% of the insurance industry" it is simply the overseer at the holding company level of just a handful of U.S. companies. It is not the functional insurance regulator for even 1% of the industry. It seems to me that both the Fed and the FIO ought to take all of their cues from the folks doing the actual regulating on a day-to-day basis.

The reporting requirements included in this draft bill would provide the public and industry with the opportunity to comment on proposed final international standards, covered agreements, and the Fed

and Treasury analyses. While having a comment period is pretty standard, many times it is actually just a formality. Do you believe these opportunities are beneficial and necessary?

How about you Mr. Thompson- Do you believe that greater transparency through public comment periods and congressional oversight would improve the rulemaking process?

Mr. Thompson – I do think the comment process is important. While we do have concerns that our comments could ultimately just be ignored, our greater concern is that many of the decisions being made are being made behind closed doors. It is critical that the proposals being considered are fully understood and for that there must be as much sunlight as possible. I also think that the transparency provisions being considered in Chairman Luetkemeyer's discussion draft might have the additional beneficial effect of ensuring that our federal officials participating in international talks are on notice that there is a lot of Congressional interest and there will be a lot of scrutiny of their activities. I don't need to tell you how that can have a salutary effect on behavior.

For either Mr. Thomson or Mr. Torti- How does this language ease the concerns of U.S. based insurers and State regulators?

Mr. Thompson – Admittedly, if everything in the current discussion draft became law tomorrow, I would still have concerns regarding international standard-setting activity for insurance regulation. To date, I have heard no real justification of the need for these types of one-size-fits-all standards and I'm skeptical of the real need for any of it. That being said, I would be more comfortable if the bill were strengthened in three key ways:

- Clearly acknowledge that any international standard is not self-executing and is entirely without legal effect in the United States until implemented through a federal or state legislative or regulatory process.
- Add language that prohibits U.S. representatives from agreeing to standards which would require any additional changes to current state or federal law.
- Revisit the inclusion of covered agreements under all of the bill's processes and requirements.