Obama Calls for ‘Office of National Insurance’

By Editor Test *Tue, Jun 23, 2009*

While the administration's June 18 report, "Financial Regulatory Reform," did not offer the “optional federal charter” that large insurance companies support as an alternative to state-by-state regulation, it did not rule one out.

The blueprint for tighter oversight of the U.S. financial sector that the Obama administration released last week provided for the establishment of an unprecedented Office of National Insurance (ONI) within the Treasury Department.

And while the report did not offer the “optional federal charter” that large insurance companies support as an alternative to state-by-state regulation, it did not rule one out.

The ONI would “gather information, develop expertise, negotiate international agreements, and coordinate policy in the insurance sector,” said the blueprint, officially called “Financial Regulatory Reform, A New Foundation: Rebuilding Financial Supervision and Regulation.”

The recommendation was based on the assumption that the insurance industry is too large and too inter-connected with the rest of the financial system-and too global-for the federal government to leave its regulation up to the individual states.

The 100-page report also for the ONI to “recommend to the Federal Reserve any insurance companies that the [ONI] believes should be supervised as “Tier 1 FHCs.” That is, financial holding companies whose failure could threaten the entire system.

“The current crisis highlighted the lack of expertise within the federal government regarding the insurance industry,” the report said. “While AIG’s main problems were created outside of its traditional insurance business, significant losses arose inside its state-regulated insurance companies as well.

“Insurance is a major component of the financial system,” the text continued. “In 2008, the insurance industry had $5.7 trillion in assets, compared with $15.8 trillion in the banking sector. There are 2.3 million jobs in the insurance industry, making up almost a third of all financial sector jobs.

“For over 135 years, insurance has primarily been regulated by the states, which has led to a lack of uniformity and reduced competition across state and international boundaries, resulting in inefficiency, reduced product innovation, and higher costs to consumers,” the report said.

Six principles for oversight
Treasury supports the following six principles for insurance regulation, according to the report:

1. *Effective systemic risk regulation with respect to insurance.* The steps proposed in this report, if enacted, will address systemic risks posed to the financial system by the insurance industry. However, if additional insurance regulation would help to further reduce systemic risk or would increase integration into the new regulatory regime, we will consider those changes.

2. ***Strong capital standards and an appropriate match between capital allocation and liabilities for all insurance companies.*** Although the current crisis did not stem from widespread problems in the insurance industry, the crisis did make clear the importance of adequate capital standards and a strong capital position for all financial firms. Any insurance regulatory regime should include strong capital standards and appropriate risk management, including the management of liquidity and duration risk.

3. ***Meaningful and consistent consumer protection for insurance products and practices.*** While many states have enacted strong consumer protections in the insurance marketplace, protections vary widely among states. Any new insurance regulatory regime should enhance consumer protections and address any gaps and problems that exist under the current system, including the regulation of producers of insurance.

4. ***Increased national uniformity through either a federal charter or effective action by the states.*** Our current insurance regulatory system is highly fragmented, inconsistent, and inefficient. While some steps have been taken to increase uniformity, they have been insufficient. As a result there remain tremendous differences in regulatory adequacy and consumer protection among the states. Increased consistency in the regulatory treatment of insurance – including strong capital standards and consumer protections – should enhance financial stability, increase economic efficiency and result in real improvements for consumers.

5. ***Improve and broaden the regulation of insurance companies and affiliates on a consolidated basis, including those affiliates outside of the traditional insurance business.*** As we saw with respect to AIG, the problems of associated affiliates outside of a consolidated insurance company's traditional insurance business can grow to threaten the solvency of the underlying insurance company and the economy. Any new regulatory regime must address the current gaps in insurance holding company regulation.

6. ***International coordination.*** Improvements to our system of insurance regulation should satisfy existing international frameworks, enhance the international competitiveness of the American insurance industry, and expand opportunities for the insurance industry to export its services.

Comments from interested parties

The National Association of Insurance Commissioners, in a statement from president CEO Theresa (Terri) M. Vaughn, Ph.D., said, "While no one proposal is completely perfect, our initial read of the Administration's financial overhaul plan seems to reflect what is most important to us: preserving the consumer protections and financial solvency oversight of the historically strong and solid system of state-based insurance regulation."

American Council of Life Insurers president and CEO Frank Keating said "ACLI therefore appreciates Treasury's commitment to work towards modernization of insurance regulation based on the principles of national uniformity, efficiency, effective oversight of systemic risk and better international cooperation. The White Paper identifies a federal charter as one possible way to achieve those objectives. ACLI strongly supports an optional federal charter as the only way to achieve them.

In commenting on the report, James Hamilton, a CCH analyst at Wolters Kluwer Law & Business, noted that the recommended Financial Stability Council “would also be able to propose regulations of financial instruments that are designed to look like insurance products, but that in reality are financial products that could present a systemic risk. But the legislation does not preempt state law governing traditional insurance products.”

Fred Joseph, president of the North American Securities Administrators Association, in a statement, praised the fact that the administration was “calling for a council of regulators to assist the Federal Reserve in monitoring risk throughout our financial system; addressing the pressing need for a fiduciary standard of care for broker-dealers providing investment advice and calling for legislation empowering the SEC to prohibit mandatory arbitration clauses in broker-dealer and investment adviser contracts with retail investors.”