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June 10, 2010

The Honorable Barney Frank
HR 4173 Conference Committee Chairman

The Honorable Christopher Dodd

HR 4173 Conference Committee Members

Re: Deregulation of existing insurance solvency, other standards, in HR 4173

Dear Chairman Frank, Senator Dodd, and Conferees:

We are writing to urge adoption by the conference committee of the House-passed language establishing a "Federal Insurance Office" (FIO), with three clarifications based on an amendment offered but not voted on in the Senate, in order to preserve state regulators' ability to protect insurance consumers. The Senate-approved version of an "Office of National Insurance" (ONI) could inadvertently result in the deregulation of state insurance oversight, including important state solvency measures.

Those Senate ONI provisions would authorize the Treasury Department to preempt existing state insurance consumer protections, including on solvency, based on international agreements establishing insurance regulatory policy that Treasury would be authorized to enter into without congressional approval. In sum, these provisions would newly empower Treasury to weaken existing state insurance regulation in the name of expanding access for foreign insurance firms to the U.S. market. Certainly this is not what the American public is demanding from the financial reform package. Adopting the House FIO language with the requested improvements could ensure that financial re-regulation legislation does not include provisions which promote *new deregulation* of the insurance industry and threaten existing state-level consumer protections.

Both versions of the bill create an insurance office in the Treasury Department that is newly empowered to negotiate agreements internationally on insurance regulatory matters, and to determine when such agreements should preempt state laws.

Negotiations on the House side resulted in language that more carefully defines what sort of agreements Treasury would be authorized to establish, that limits the scope of preemption to state laws that directly result in discrimination against foreign firms, and that requires greater transparency and an enhanced role for Congress. These improvements were designed to ensure that Treasury would have authority to participate in international negotiations on insurance regulatory matters while preserving the ability of state regulators and lawmakers to maintain strong insurance consumer and solvency protections.

The House bill should be improved with three fixes drawn from Senate amendment 3922, offered by Senator Merkley and others, which never received a vote on the Senate floor. Senate amendment 3922 replicated the House improvements and additionally clarified that preemption authority is limited to the extent of the less favorable treatment of a foreign insurer subject to a covered agreement. The amendment also further clarified the definition of agreements into which Treasury may enter by requiring that they protect insurance consumers in the United States, promote the integrity and stability of the financial system and required consultation with state regulators during the negotiation of such pacts. Finally, the Senate amendment clarified that only state laws that are facially discriminatory (not those treating foreign and domestic firms the same that may have an unintended disparate effect) may be preempted.

The House bill narrows the scope of insurance agreements Treasury may negotiate to *recognition agreements*, which recognize a foreign jurisdiction's regulations in a specific area as sufficient to meet U.S. policy goals. The Senate bill grants Treasury broad authority to usurp Congress' role by diplomatically legislating de novo U.S. policy on any prudential matter to set a ceiling on state rules. Despite an effort through a savings clause to wall off some of the central consumer protections in state insurance law, the broad authority provided in the Senate bill threatens to weaken important state oversight, including with respect to solvency regulation. We urge you to support the House's narrower definition. It should be further clarified by requiring that such agreements promote consumer protection and financial stability. The Senate bill does not prevent Treasury-negotiated agreements from undermining the consumer protection and financial stability goals of state laws they would override.

The scope of preemption must also be clarified, to help ensure that state laws actually treat a foreign insurer unfairly in order to be overturned. The Senate bill would base preemption decisions on the "results" of a law. Yet, insurance laws and regulations regularly have different outcomes for different companies, due to their individual business decisions. If the current Senate language stands, many facially neutral state insurance protections would be exposed to preemption in favor of lower international standards. The House bill moved towards fixing this serious problem. We urge that this standard be further clarified to require a state law "directly treat" a foreign insurer less favorably than a U.S. insurer in order to be preempted. The same fix must be made in the savings clause intended to protect state capital and solvency rules, to ensure that existing solvency rules remain in effect for domestic insurers. In addition, we request that the savings clause provision relating to solvency measures be clarified with respect to the extent of preemption. This could be achieved by inserting at the end of that provision the language: "and in that case only to the extent of the less favorable treatment of the non-United States insurer domiciled in a foreign jurisdiction that is subject to a Covered Agreement".

The House made additional improvements that should be preserved, including:

- Requiring consultation with Congress as agreements are negotiated, (state regulators should be consulted as well);
- Granting states the right to substantive judicial review of preemption decisions;
- Ensuring existing deregulatory trade agreement financial service provisions cannot be used to preempt state laws;
- Requiring public notice of preemption decisions;
- And, preempting state laws only on the basis of agreements negotiated prospectively.

The Senate bill's Office of National Insurance could reverse more than sixty years of regulation

in the fifty states and Territories. Its replacement would be regulation by Treasury fiat, with new standards negotiated by Treasury in the international arena and behind closed doors without congressional approval, which would then be used to determine piecemeal which state laws are weakened and which survive. Such decisions would be implemented through a mere posting of decisions in the Federal Register and not be subject to challenge on the merits.

We urge your support for the House bill, with the adjustments outlined above, to ensure that the end result of Congress's efforts to reform the financial system is not deregulation of the insurance industry. While nearly 600 banks used funds from the Troubled Assets Relief Program (TARP), only three insurers obtained such assistance. AIG's high-profile collapse was unquestionably due to the actions, and failed federal oversight, of its derivatives trading arm, not its state-regulated insurance companies. Certainly the American public would be outraged if Congress' re-regulation efforts resulted in new deregulation of insurance solvency standards that worked, thus exposing us to the risk of further bailouts.

Thank you for considering our concerns on behalf of insurance consumers across the country.

Sincerely,

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Consumer Watchdog

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