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Insurance Regulation: Background, Overview, and Legislation in the 114th Congress

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Summary

The individual states have been the primary regulators of insurance since 1868. Following the 1945 McCarran-Ferguson Act, this system has operated with the explicit blessing of Congress, but has also been subject to periodic scrutiny and suggestions that the time may have come for Congress to reclaim the regulatory authority it granted to the states. In the late 1980s and early 1990s, congressional scrutiny was largely driven by the increasing complexities of the insurance business and concern over whether the states were up to the task of ensuring consumer protections, particularly insurer solvency.

Immediately prior to the 2007-2009 financial crisis, congressional attention on insurance regulation focused on the inefficiencies in the state regulatory system. A major catalyst was the aftermath of the Gramm-Leach-Bliley Act of 1999 (GLBA), which overhauled the regulatory structure for banks and securities firms, but left the insurance sector largely untouched. Many larger insurers, and their trade associations, had previously defended state regulation but considered themselves at a competitive disadvantage in the post-GLBA regulatory structure. Various pieces of insurance regulatory reform legislation were introduced, including bills establishing a broad federal charter for insurance as well as narrower, more targeted bills.

The financial crisis refocused the debate surrounding insurance regulatory reform. Unlike many financial crises in the past, insurers played a large role in this crisis. In particular, the failure of the insurer American International Group (AIG) spotlighted sources of risk that had gone unrecognized. The need for a systemic risk regulator for the entire financial system was a common thread in many of the post-crisis financial regulatory reform proposals. The Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-203), enacted following the crisis, gave enhanced systemic risk regulatory authority to the Federal Reserve and to a new Financial Stability Oversight Council (FSOC). Three insurers have since been designated as Systemically Important Financial Institutions (SIFIs) although one of these designations has been overturned in federal court. The Dodd-Frank Act also included measures affecting the states' oversight of surplus lines insurance and reinsurance and the creation of a new Federal Insurance Office (FIO) within the Department of the Treasury.

The states, particularly working through the National Association of Insurance Commissioners (NAIC), have generally not been idle following congressional attention. They reacted quickly to GLBA requirements that related to insurance agent licensing and to the changes enacted in Dodd-Frank, including engaging with the FSOC and FIO. The regulatory initiatives undertaken by the NAIC since the financial crisis include increased oversight of holding companies and new enterprise risk management requirements. Because enactment by the state legislature is necessary before the NAIC's suggested legal changes can take effect in that state, the process typically does not move rapidly.

Among the insurance regulatory issues addressed by legislation in the 114th Congress are the licensing of insurance agents and brokers (H.R. 26/P.L. 114-1), the degree of the authority of the Federal Reserve and the Federal Deposit Insurance Corporation (FDIC) over insurers (H.R. 1478/S. 798), and international insurance standards (S. 1086, H.R. 2141, H.R. 5143, and H.R. 6436). S. 1484/S. 1910 and H.R. 5983, broader bills addressing financial regulation, also include provisions on the latter two topics and would modify the SIFI designation process. In addition, other international issues have been of concern to Congress, such as the European Union's Solvency II project to overhaul the European insurance regulatory system and the U.S. state requirements on non-U.S. insurers for reinsurance collateral.

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Background

Insurance companies constitute a major segment of the U.S. financial services industry. The industry is often separated into two parts: *life and health insurance companies*, which also often offer annuity products, and *property and casualty insurance companies*, which include most other lines of insurance, such as homeowners insurance, automobile insurance, and various commercial lines of insurance purchased by businesses. Premiums for life and health companies in 2015 totaled $593.7 billion with assets totaling $6.40 trillion. Premiums for property and casualty insurance companies totaled $518.4 billion with assets totaling $1.81 trillion.[1]

Different lines of insurance present very different characteristics and risks. Life insurance typically is a longer-term proposition with contracts stretching over decades and insurance risks that are relatively well defined in actuarial tables. Property/casualty insurance typically is a shorter-term proposition with six-month or one-year contracts and greater exposure to catastrophic risks. Health insurance has evolved in a very different direction, with many insurance companies heavily involved with health care delivery, including negotiating contracts with physicians and hospitals, and a regulatory system much more influenced by the federal government through the Medicare, Medicaid, the Employee Retirement Income Security Act of 1974 (ERISA),[2] and the Patient Protection and Affordable Care Act (ACA).[3] This report concentrates primarily on property/casualty and life insurance.[4]

Insurance companies, unlike banks and securities firms, have been chartered and regulated solely by the states for the past 150 years. Legal and legislative landmarks in the state-based insurance regulatory system have included Supreme Court decisions in 1868 (*Paul v. Virginia*)[5] and 1944 (*U.S. v. South-Eastern Underwriters Association*)[6] and federal legislation in 1945 (the McCarran-Ferguson Act).[7] The McCarran-Ferguson Act specifically preserved the states' authority to regulate and tax insurance and also granted a federal antitrust exemption to the insurance industry for "the business of insurance." (The evolution of insurance regulation is presented in greater detail in **Appendix A**; a legal analysis of the constitutionality of federal regulation of insurance can be found in **Appendix B**.)

Since the passage of McCarran-Ferguson, both Congress and the federal courts have taken actions that have somewhat expanded the reach of the federal government into the insurance sphere.[8] The insurance industry has often been divided over the possibility of federal actions affecting insurance. The states typically, though not always, have resisted federal actions, arguing that the states are better positioned to regulate insurance and address consumer complaints and that states have engaged in concerted actions to address concerns raised at the federal level. The two large

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[1] Premium amounts used are net premiums written and asset amounts are admitted assets from A.M. Best, *Statistical Study: U.S. Property/Casualty - 2015 Financial Results*, March 21, 2016, and A.M. Best, *Statistical Study: U.S. Life/Health - 2015 Financial Results*, March 13, 2016.

[2] P.L. 93-406; 88 Stat. 829.

[3] P.L. 111-148; 124 Stat. 119.

[4] For more information on health insurance, see CRS Report RL32237, *Health Insurance: A Primer*, by Bernadette Fernandez and Namrata K. Uberoi.

[5] *Paul v. Virginia*, 75 U.S. (8 Wall.) 168 (1868).

[6] *U.S. v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944).

[7] Codified at 15 U.S.C. §1011 *et seq*.

[8] For more information on court decisions, see CRS Report RL33683, *Courts Narrow McCarran-Ferguson Antitrust Exemption for "Business of Insurance": Viability of "State Action" Doctrine as an Alternative*, by Janice E. Rubin.

legislative overhauls of financial regulation in the past two decades, the Gramm-Leach-Bliley Act of 1999 (GLBA)[9] and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank),[10] expanded the federal role in insurance, but the states continued as the primary regulators of insurance following these acts.

GLBA removed legal barriers between securities firms, banks, and insurers, allowing these firms to coexist under a financial holding company structure. Under the act, such a holding company was overseen by an umbrella regulator—the Federal Reserve for holding companies that included bank subsidiaries or the Office of Thrift Supervision (OTS) for holding companies with thrift or savings association subsidiaries. Within a holding company, GLBA established a system of functional regulation for the bank, thrift, securities, and insurance subsidiaries. This meant that insurance company subsidiaries within a bank or thrift holding company were functionally regulated by state insurance authorities, with limited oversight by the federal regulator of the holding company. For more information on GLBA, see "The Gramm-Leach-Bliley Act" below.

The Dodd-Frank Act altered the post-GLBA regulatory structure, while leaving the basic functional regulatory paradigm largely the same. The act gave enhanced systemic risk regulatory authority to the Federal Reserve and to a new Financial Stability Oversight Council (FSOC), including some oversight authority over insurers. The authority to oversee holding companies, including those with insurance subsidiaries, was consolidated in the Federal Reserve with additional capital requirements added. The Dodd-Frank Act also included measures affecting the states' oversight of surplus lines insurance and reinsurance and the creation of a new Federal Insurance Office (FIO) within the Department of the Treasury.[11]

Legislation in the 114th Congress

Insurance regulatory issues before the 114th Congress include

- overseeing the implementation of, and possible amendments to, the Dodd-Frank Act, including specific legislation, such as H.R. 1478/S. 798, and provisions in S. 1484/ S. 1910, which would limit the Federal Reserve and Federal Deposit Insurance Corporation (FDIC) authority over insurers and H.R. 5983, which would merge and revamp the FIO and the independent insurance expert position on FSOC;
- legislation that would narrowly reform the current regulatory system, such as Title II of H.R. 26/P.L. 114-1, which attempts to streamline the state regulation of insurance producer licensing; and
- responding to international developments, such as the changes to the European Union's regulatory scheme known as Solvency II and the development of international standards by the International Association of Insurance Supervisors (IAIS). Legislation addressing U.S. involvement in the IAIS includes S. 1086, H.R. 2141, H.R. 5143 and H.R. 6436 as well as provisions in S. 1484/S. 1910.

[9] P.L. 106-102; 113 Stat. 1338.

[10] P.L. 111-203; 124 Stat. 1376.

[11] For more information on the specific insurance provisions in the Dodd-Frank Act, see CRS Report R41372, *The Dodd-Frank Wall Street Reform and Consumer Protection Act: Insurance Provisions*, by Baird Webel.

This report provides background on these issues as well as others that may be of congressional interest. It includes summaries and analysis of federal legislation and executive actions as well as policies undertaken at the state and international level.

Enacted Legislation

National Association of Registered Agents and Brokers Reform Act (H.R. 26/P.L. 114-1, Title II)[12]

The National Association of Registered Agents and Brokers Reform Act of 2015 was introduced by Representative Randy Neugebauer on January 6, 2015, as Title II of H.R. 26. It was identical to an amended version of S. 2244 in the 113th Congress, which passed the House on December 10, 2014. H.R. 26 passed the House on January 7, 2015, passed the Senate on January 8, 2015, and was signed by the President (P.L. 114-1) on January 12, 2015.

As enacted, the National Association of Registered Agents and Brokers Reform Act establishes a National Association of Registered Agents and Brokers (NARAB).[13] The association is to be a private, nonprofit corporation. Its members, required to be licensed as insurance producers in a single state and meet other requirements, will be able to operate in any other state subject only to payment of the licensing fee in that state, rather than having to obtain a separate license in the additional states, as is often the case now. The association members will still be subject to each state's consumer protection and market conduct regulation, but individual state laws that in certain respects treat out-of-state insurance producers differently from in-state producers are preempted. The NARAB will be overseen by a board made up of five appointees from the insurance industry and eight from the state insurance commissioners. The appointments are to be made by the President subject to Senate confirmation, and the President is empowered to dissolve the board as a whole or suspend individual members for cause or suspend the implementation of any rule or action taken by the association. Ten members of the NARAB board have been appointed by the President, but none have been acted on by the Senate.

House- or Senate-Passed Legislation

Transparent Insurance Standards Act of 2016 (H.R. 5143)

H.R. 5143 was introduced by Representative Blaine Luetkemeyer on February 25, 2016. It was marked up and ordered reported by the House Committee on Financial Services on a vote of 34-25 on June 16, 2016, and was reported (H.Rept. 114-831) on November 22, 2015. CBO scored the bill, finding it would increase spending by a total of $7 million over 10 years.[14] This amount was to be offset through a reduction in the Securities and Exchange Commission Reserve Fund

[12] For more information, please see CRS Report R43095, *Insurance Agent Licensing: Overview and Background on Federal NARAB Legislation*, by Baird Webel.

[13] This is the second time that a "NARAB" has appeared in statute. The Gramm-Leach-Bliley Act, P.L. 106-102, Title III, Subtitle C, included the provisional creation of a NARAB to streamline state insurance producer licensing for agents and brokers. The GLBA NARAB provisions, however, were not to go into effect if a majority of the states enacted uniformity in their insurance producer licensing laws and reciprocity for nonresident producer licensing laws. The states as a whole met these GLBA requirements, but some individual states never adopted reciprocity legislation.

[14] Congressional Budget Office, Cost Estimate: H.R. 5143 Transparent Insurance Standards Act of 2016 as ordered reported by the House Committee on Financial Services on June 16, 2016, August 31, 2016, at https://www.cbo.gov/publication/51949.

added by the House Committee on Rules prior to consideration on the floor.[15] H.R. 5143 was passed by the House on December 7, 2016, on a vote of 239-170. The White House released a Statement of Administration Policy indicating that presidential advisors would recommend a veto of the bill.[16]

In general, H.R. 5143 would bolster the primacy of the state-based insurance regulatory system and would increase public and congressional input into the negotiation of international insurance standards and covered agreements. H.R. 5143 lists specific U.S. objectives regarding international standards, such as ensuring that the Treasury and the Fed achieve consensus positions with the states, promoting the regulatory standards used in the United States, and ensuring transparency in international organizations and international standards. Beyond these general goals, H.R. 5143 creates specific procedural requirements for the adoption of international standards and covered agreements as well as augmenting the authorities of the FSOC independent insurance expert.

Internationals Standards

Prior to the agreement to or adoption of international standards generally:

- The Treasury, Fed, and state insurance commissioners would be required to publish the standards and provide at least 30 days' public comment period.
- The Treasury and Fed would be jointly required to analyze the effect of the standards and report on the analysis. The report would be subject to public comment for at least 60 days and would be reviewed by the Comptroller General.
- The Treasury and Fed must certify that the proposed standards would not result in any change in state law.

If the standards involve capital requirements, additional requirements would apply:

- The Fed must have previously issued its rules for domestic capital requirements.
- The standards must be consistent with both state and Fed capital standards.
- The Fed and Treasury must certify that these capital standards are solely designed to ensure that funds are available to pay policyholder claims.

Any proposed standard must be submitted to Congress and lay over for a period of 90 calendar days. This period may run consecutively with the public comment periods.

H.R. 5143 would also require the Treasury and Fed to provide semi-annual testimony and reports on international activities and a specific report on transparency and the IAIS. The Comptroller General would also be tasked with a report on the transparency of domestic organizations acting as a designee of the states, which would appear to be applicable primarily to the NAIC.

Covered Agreements

H.R. 5143 would add a 30-day public notice and comment requirement as well as a requirement that FIO and USTR "consult with and directly include State insurance commissioners."

[15] See the House Rules Committee website, "Summary of Modification," at https://rules.house.gov/bill/114/hr-5143.

[16] Executive Office of the President, *STATEMENT OF ADMINISTRATION POLICY:* H.R. 5143– *Transparent Insurance Standards Act of 2016*, December 6, 2016, at https://www.whitehouse.gov/sites/default/files/omb/legislative/sap/114/saphr5143h_20161206.pdf.

FSOC Independent Insurance Expert

Current statute is largely silent on specific authorities of the FSOC independent insurance expert. H.R. 5143 adds the authority to consult with international bodies and attend international groups.

Committee-Reported Legislation

Financial Regulatory Improvement Act of 2015 (S. 1484/Title IX of S. 1910)[17]

On May 12, Chairman Richard Shelby of the Senate Committee on Banking, Housing, and Urban Affairs released a discussion draft of this unnumbered bill, which was marked up on May 21, 2015. The committee ordered the bill reported to the full Senate on a vote of 12-10 and it was assigned S. 1484 when introduced on June 2, 2015. The Financial Regulatory Improvement Act was also included as Title IX of Senator John Boozman's S. 1910, the Financial Services and General Government Act, 2016. S. 1910 was reported (S.Rept. 114-97) by the Senate Committee on Appropriations on July 30, 2015. The insurance provisions contained in Title IX of S. 1910 were not included in the Consolidated Appropriations Act, 2016.[18]

The Financial Regulatory Improvement Act of 2015 includes sections addressing a wide variety of financial-sector issues. Title IV of S. 1484 includes three sections directly addressing insurance. Section 401 is a Sense of Congress reaffirming the 1945 McCarran-Ferguson Act, which created the current, state-centered system of insurance regulation. Section 402 contains language similar to S. 798. Section 402(a) is identical to S. 798 and would require the specific consent of individual state insurance regulators before insurance company assets could be moved as part of Fed oversight of thrift holding companies. This language parallels current law as it applies to bank holding companies. Section 402(b) is slightly different than S. 798. Under this section, the FDIC could only access insurance company assets during orderly liquidation of a financial institution under the Dodd-Frank Act only (1) in order to secure repayment of funds and (2) if the FDIC, in consultation with the state insurance commissioners determines that the lien would not "unduly impede or delay the liquidation or rehabilitation of the insurance company, or the recovery by its policyholders."[19] Section 403 contains language similar to S. 1086, which would require additional reporting and consultative measures surrounding ongoing international negotiations to create insurance regulatory standards.

In addition to the insurance-focused Title IV, Title III addresses the designation of nonbank financial companies as systemically important, which has been a major concern of insurers since Dodd-Frank. The bill would require FSOC to provide more information to institutions and give them more opportunities to take actions to avoid or reverse SIFI designation. It would also increase public disclosure requirements surrounding the designation process.

Financial CHOICE Act of 2016 (H.R. 5983)

H.R. 5983 was introduced by House Committee on Financial Services Chairman Jeb Hensarling on September 9, 2016, and marked up and ordered reported on a vote of 30-26 on September 13, 2016. The bill was also referred to the House Committees on Agriculture, Ways and Means, the

[17] For more information see CRS In Focus IN10332, *Financial Stability Oversight Council: Issues in the Financial Regulatory Improvement Act of 2015*, by Edward V. Murphy (available to congressional clients upon request).

[18] P.L. 114-113.

[19] S. 1484, §402(b)(2).

Judiciary, Oversight and Government Reform, Transportation and Infrastructure, Rules, the Budget, and Education and the Workforce.

H.R. 5983 is a wide-ranging bill that would change many parts of the financial regulatory system.[20] Title V of H.R. 5983 would amend Dodd-Frank to effectively merge Treasury's Federal Insurance Office and the FSOC's independent member with insurance expertise. (See "Federal Insurance Office" and "FSOC and SIFI Designation" below) In their place, the FCA would create the Office of Independent Insurance Advocate, a new independent bureau within Treasury, with the head appointed by the President and confirmed by the Senate. The Independent Insurance Advocate would be a voting member of FSOC and the office would take over many, but not all, of the duties of the FIO director. Such changes would include the advocate would have the authority to *observe* the insurance industry, rather than FIO's charge to *monitor* the insurance industry; the advocate would not be charged with monitoring the access of underserved communities to insurances, as FIO currently is; and the advocate would not have the authority to require the submission of data from the industry that FIO currently has. H.R. 5983 would also add an additional public notice and comment period for any covered agreement.

Introduced Legislation

Policyholder Protection Act of 2014 (H.R. 1478/S. 798)[21]

Representative Bill Posey and Senator David Vitter introduced H.R. 1478 and S. 798 respectively on March 19, 2015. Language similar to S. 798 was included in S. 1484/Title IX of S. 1910 as discussed below.

Under current law, an insurer that is a bank holding company or an affiliate of a bank holding company may not be required to "provide funds or other assets"[22] of the insurer to an affiliated depository institution if the insurer's state regulator determines that providing such assistance "would have a material adverse effect on the financial condition of the insurance company."[23] S. 798 would extend this provision to cover any insurance company that is a savings and loan holding company and to any other company that is an insurance company and that "directly or indirectly controls" an insured depository institution. The bill, moreover, includes a rule of construction that may have the effect of extending the provision more broadly. Under current law, it covers situations in which an insurance company is required to "provide funds or other assets" to an affiliated insured depository institution. The rule of construction in the bill would extend coverage to the Federal Reserve's requiring the specified insurance entity to be "a source of financial strength" for an affiliated depository institution. The four entities that are covered, provided they are insurance companies, are any bank holding company, any savings and loan holding company, any affiliate of an insured depository institution, or any company that "directly or indirectly controls an insured depository institution."

H.R. 1478/S. 798 also has provisions addressing the FDIC authority over insurers under Title II of the Dodd-Frank Act. The bill would require the FDIC to notify the applicable state insurance regulator before placing a lien on and thereby accessing insurance subsidiary assets during an FDIC-administered orderly liquidation of a financial holding company. If the state regulator

[20] For more information see CRS Report R44631, *The Financial CHOICE Act: Policy Issues*, coordinated by Sean M. Hoskins.

[21] The following summary was authored by CRS Legislative Attorney Maureen Murphy.

[22] 12 U.S.C. §§1844(g)(1)-(2).

[23] 12 U.S.C. §§1844(g)(1)-(2).

notifies the FDIC that placing a lien on the assets would have a "materially adverse effect" on policyholders, the FDIC would have no authority to place such a lien. In addition, the bill addresses a provision in current law that allows the FDIC to step into the shoes of the state regulator in the case of an insurance company failure. Current law specifies that the state insurance regulator is to conduct the liquidation or *rehabilitation* of such an insurance company. This law grants FDIC backup authority if the state regulator has not filed a suit in state court for *orderly liquidation*, but does not expressly mention a suit for rehabilitation. The bill would make it clear that the FDIC could only exercise backup authority if the state regulator fails to file suit for either orderly liquidation or rehabilitation.

International Insurance Capital Standards Accountability Act of 2015 (S. 1086)

S. 1086 was introduced by Senator Dean Heller and Senator Jon Tester on April 28, 2015. It was referred to the Senate Committee on Banking, Housing, and Urban Affairs. While not specifically on S. 1086, the committee also held a hearing the same day on "The State of the Insurance Industry and Insurance Regulation" and the Subcommittee on Securities, Insurance, and Investment held a hearing on "Examining Insurance Capital Rules and FSOC Process" on April 30, 2015. Language similar to S. 1086 was included in S. 1484/Title IX of S. 1910, as discussed below.

S. 1086 would create an "Insurance Policy Advisory Committee on International Capital Standards and Other Insurance Issues" at the Federal Reserve made up of 21 members with expertise on various aspects of insurance. It would require a report and testimony from the Federal Reserve and the U.S. Department of the Treasury on the ongoing discussions at the IAIS on an annual basis until 2018. The Federal Reserve and FIO would be required to complete a study and report, along with the opportunity for public comment and review by the Government Accountability Office (GAO), on the impact of international capital standards or other proposals prior to agreeing to such standards.

International Insurance Standards Transparency and Policyholder Protection Act (H.R. 2141)

H.R. 2141 was introduced by Representative Sean Duffy on April 30, 2015. It was referred to the House Committee on Financial Services. This bill would set negotiating objectives for U.S. representatives in international insurance capital standard negotiations, which are currently ongoing at the IAIS. The objectives are largely based on the current approach used in the United States including a focus on protection of policyholders, regulation on a legal entity basis, and use of supervisory colleges in the oversight of insurance groups. The bill would prohibit U.S. representatives from agreeing to an international standard unless it is "designed solely to help ensure that sufficient funds are available to pay claims to an insurer's policyholders in the event of the liquidation of that entity" except in the case of enhanced capital standards applied to insurers designated as systemically important financial institutions (SIFIs) under the Dodd-Frank Act. H.R. 2141 would also require notice and consultation with the House Committee on Financial Services and Senate Committee on Banking, Housing, and Urban Affairs before and during the process of international negotiations. The U.S. Department of the Treasury's Federal Advisory Committee on Insurance and the National Association of Insurance Commissioners (NAIC) are also to be consulted during the negotiations and the GAO is to provide an assessment of any agreement that is reached.

Captive Insurers Clarification Act (S. 1561)

S. 1561 was introduced by Senator Patrick Leahy on June 11, 2015. It was referred to the Senate committee on Banking, Housing, and Urban Affairs. The bill would amend the Nonadmitted and Reinsurance Reform Act of 2010 (Title V, Subtitle B of Dodd-Frank) to exclude captive insurers from the definition of *a nonadmitted insurer* and thus excluding captives from the regulatory and tax requirements in the act (see "Surplus Lines and Reinsurance" below). A captive insurance company would be defined as an insurance company wholly owned directly or indirectly (1) by a single-parent company and whose primary purpose is to insure the risks of that single-parent company or its affiliates; (2) by a group of companies and whose primary purpose is to insure the risks of that group or its affiliates; and (3) by an industry, trade, or service group or association, and whose primary purpose is to insure the risks of any member in that group or association, including any member affiliate.

Claims Licensing Advancement for Interstate Matters Act (H.R. 2998)

H.R. 2998 was introduced on July 9, 2015, by Representative Stephen Fincher. It was referred to the House Committee on Financial Services. This bill would preempt state laws requiring claims adjuster licensing and allow insurance claims adjusters to apply for membership in the National Association of Registered Agents and Brokers (created in P.L. 114-1) and thus operate in multiple states under NARAB. This preemption would only apply four years after enactment and only for states that do not enact laws allowing for uniformity and reciprocity in claims adjuster licensing. It would not apply to states that do not require license for claims adjusting.

Nonprofit Property Protection Act (H.R. 3794)

H.R. 3794 was introduced by Representative Dennis Ross on October 21, 2015. It was referred to the House Committee on Financial Services. This bill would expand the insurance allowed under the preemption to state law in the federal Liability Risk Retention Act to include all forms of commercial insurance, excluding health, life, or disability insurance or workers compensation insurance.[24] This expansion would only apply to risk retention groups organized and operated by Section 503(c) nonprofits, licensed in the United States, and meeting additional operating criteria.

U.S. Insurance Regulation Works Act of 2016 (H.R. 6436)

H.R. 6436 was introduced by Representative Denny Heck on December 5, 2016. It was referred to the House Committee on Financial Services. This bill would require that any international insurance standards agreed to by representatives of the federal government reflect existing federal and state laws, particularly the "primacy of policyholder protection in solvency regulation." It would also direct federal representatives to consult with and seek to include state insurance commissioners in international fora regarding insurance issues.

Implementation of the Dodd-Frank Act

Federal Insurance Office

Title V, Subtitle A of the Dodd-Frank Act created the Federal Insurance Office inside of the Department of the Treasury. FIO is to monitor all aspects of the insurance industry and coordinate

[24] 15 U.S.C. §§3901-3906.

and develop policy relating to international agreements. It has the authority to preempt state laws and regulations when these conflict with international agreements. This preemption authority is limited, applying only when the state measure (1) results in less favorable treatment of a non-U.S. insurer compared with a U.S. insurer, and (2) is inconsistent with a written international agreement regarding prudential measures. Such an agreement must achieve a level of consumer protection that is "substantially equivalent"[25] to the level afforded under state law. FIO preemption authority does not extend to state measures governing rates, premiums, underwriting, or sales practices, nor does it apply to state coverage requirements or state antitrust laws. FIO preemption decisions are also subject to *de novo* judicial review under the Administrative Procedure Act.[26] The monitoring function of FIO includes information gathering from both public and private sources. This is backed by subpoena power if the director issues a written finding that the information being sought is necessary and that the office has coordinated with other state or federal regulators that may have the information.[27]

FIO is headed by a director, which is a career SES position, not a presidential appointment. Michael McRaith, previously Illinois insurance commissioner, currently serves as the head of FIO. The office has issued several reports[28] and has been active in international fora.[29] Director McRaith and the United States Trade Representative notified Congress in November 2015 that negotiations on a covered agreement with the European Union were commencing, but no agreement has been reached.

Systemic Risk Provisions

The Dodd-Frank Act provides for systemic risk provisions that potentially affect the insurance industry through enhanced Federal Reserve oversight and higher prudential standards for financial firms deemed SIFIs, and through resolution authority to be undertaken by the FDIC.

FSOC and SIFI Designation

All banks with greater than $50 billion in assets are considered SIFIs by statute; designation of nonbank SIFIs is done by vote of the Financial Stability Oversight Council (FSOC).[30] The FSOC is "charged with identifying risks to the financial stability of the United States; promoting market discipline; and responding to emerging risks to the stability of the United States' financial system."[31] One of the 10 voting members is a presidential appointee who is to be an expert on insurance issues.[32] The insurance representation on the FSOC is, however, exceeded significantly

[25] 31 U.S.C. §313(r)(2) as added by P.L. 111-203 §502; the law renumbered 31 U.S.C. §313 as 31 U.S.C. §312.

[26] 5 U.S.C. §551 *et seq*.

[27] This subpoena power has be of past congressional interest. In the 112th Congress, H.R. 3559, which would have limited this subpoena power, was marked up by the House Financial Services Subcommittee on Housing and Insurance and the subcommittee held a hearing on similar draft legislation in the 113th Congress (*Legislative Proposals to Reform Domestic Insurance Policy*, 113th Cong., 2nd sess., May 20, 2014).

[28] See Federal Insurance Office, "Reports and Notices," at https://www.treasury.gov/initiatives/fio/reports-and-notices/Pages/default.aspx.

[29] Director McRaith chairs the Financial Stability and Technical Committee of the International Association of Insurance Supervisors as of May 2016. See IAIS, *Committee and Subcommittee Membership List*, at http://www.iaisweb.org/page/about-the-iais/organisational-structure//file/60640/iais-committees-and-members-public.

[30] For more information on the FSOC, see CRS Report R42083, *Financial Stability Oversight Council: A Framework to Mitigate Systemic Risk*, by Edward V. Murphy.

[31] See the FSOC website at http://www.treasury.gov/initiatives/fsoc/Pages/home.aspx.

[32] In addition to the independent insurance expert, the director of FIO and one state insurance commissioner serve as

by entities whose primary regulatory focus is on depository institutions. Four of the 10 voting members, the heads of the Federal Reserve, the FDIC, the Office of the Comptroller of the Currency (OCC) and the National Credit Union Association (NCUA) have the prudential regulation of banks or other depository institutions as a primary mission, while a fifth member, the head of the Consumer Financial Protection Bureau (CFPB), has the regulation of the market conduct of banks as a primary mission. As heads of agencies or departments, the other nine voting members of FSOC also have higher organizational capacities than the insurance expert, who, at present, has a total of three staff members reporting to him.

The higher prudential standards may be set by the Federal Reserve based on various risk-related factors. The statutory standards include risk-based capital requirements that account for off-balance-sheet activities, leverage limits, liquidity requirements, risk management requirements, and exposure limits of 25% of a company's capital per counterparty. Other prudential standards may be applied at the Federal Reserve's discretion. The firms are required to submit resolution plans ("living wills") and credit exposure reports. Regulated subsidiaries continue to be regulated by their primary functional regulator (i.e., the state insurance regulators for insurers). The functional regulator, however, may be overridden if the Federal Reserve believes the firm is not adhering to regulatory standards or poses a threat to financial stability. The Federal Reserve must conduct annual stress tests on systemically significant firms and, in consultation with the FSOC and the FDIC, issue regulations establishing remediation measures to be imposed at an early stage of a firm's "financial decline" in an effort to prevent insolvency and its potential impact on the financial system.[33] As nonbank financial institutions overseen by the Federal Reserve, insurers designated as SIFIs would also fall under the Collins Amendment and Volcker Rule as discussed below.

FSOC issued a final rule detailing the criteria the FSOC would use to determine whether nonbank financial companies are systemically important. [34] The council has designated three insurers as SIFIs: AIG, Prudential Financial, and MetLife. In general, most insurers have argued that they do not pose a systemic risk due to particular facets of insurance operations, such as the longer-term nature of risks faced by insurers, a lower susceptibility to runs, and the levels of capital required by state insurance regulators.[35] The designations of Prudential Financial and MetLife were not without some controversy, with two members of FSOC voting against the Prudential designation[36] and one voting against the MetLife designation.[37] Subsequent to the designation, MetLife filed a lawsuit challenging the SIFI designation. The U.S. District Court decision found

non-voting members. The current independent insurance expert is S. Roy Woodall, Jr. See https://www.treasury.gov/initiatives/fsoc/about/council/Pages/roy_woodall.aspx.

[33] This information adapted from CRS Report R41384, *The Dodd-Frank Wall Street Reform and Consumer Protection Act: Systemic Risk and the Federal Reserve*, by Marc Labonte.

[34] Text of the final rule can be found on the FSOC website at http://www.treasury.gov/initiatives/fsoc/Documents/Nonbank%20Designations%20-%20Final%20Rule%20and%20Guidance.pdf; the Federal Register version can be found at https://www.federalregister.gov/articles/2012/04/11/2012-8627/authority-to-require-supervision-and-regulation-of-certain-nonbank-financial-companies.

[35] See, for example, comments submitted on the FSOC rule by the American Council of Life Insurers and the Property and Casualty Insurers Coalition, available at http://www.regulations.gov/#!documentDetail;D=FSOC-2011-0001-0024 and http://www.regulations.gov/#!documentDetail;D=FSOC-2011-0001-0023.

[36] Financial Stability Oversight Council, *Meeting Minutes*, September 19, 2013, available at http://www.treasury.gov/initiatives/fsoc/council-meetings/Pages/meeting-minutes.aspx.

[37] Financial Stability Oversight Council, *Meeting Minutes*, December 18, 2014, available at http://www.treasury.gov/initiatives/fsoc/council-meetings/Pages/meeting-minutes.aspx.

for MetLife and rescinded the designation. This decision was then appealed by FSOC but the appeal has not reached a final conclusion.[38]

Orderly Liquidation and the FDIC

Any financial company, not just those previously designated as SIFIs, could be subject to Dodd-Frank's special resolution regime based on a finding that its failure would cause systemic disruption. Insurance subsidiaries of such a financial company, however, would not be subject to this regime. Instead, the resolution of insurance companies would continue to be conducted in accordance with the applicable state insurance resolution system, although the FDIC would have "backup authority" to resolve insurers if the state system has not acted within 60 days of a finding. With regard to funding for the resolution of systemically important financial firms, there is no pre-funded resolution mechanism under the act. Instead, the FDIC is to impose assessments on financial companies with more than $50 billion in assets, as well as other financial firms that are overseen by the Federal Reserve, to fund the resolution of a systemically important firm in the event the assets of the failed firm are insufficient to do so. The FDIC is to impose such assessments on a risk-adjusted basis. When imposing such assessments on an insurance company, the FDIC is to take into account the insurers' contributions to the state insurance resolution regimes. The FDIC has begun issuing rules regarding the new resolution regime.[39]

Federal Reserve Holding Company Oversight

The Dodd-Frank Act consolidated oversight of thrift holding companies and bank holding companies under the Federal Reserve, when previously thrift holding companies had been overseen by the OTS. Since several insurers were, and are, thrift holding companies, these insurers experienced a change in holding company regulator due to Dodd-Frank. The act also strengthened the capital standards applied to these holding companies, particularly through Section 171, commonly known as the "Collins Amendment," after its sponsor, Senator Susan Collins. In addition to the capital requirements, insurers could also have been affected by accounting standards required by the Federal Reserve, which differ from the standards required by state insurance regulators.

Concerns were expressed by both insurers and some Members of Congress that the capital rules applied by the Federal Reserve would be identical to those applied to banks despite the difference in business models between banks and insurers.[40] The Federal Reserve, in fact, indicated that its reading of the Collins Amendment was that the statute required such identical treatment. P.L. 113-279 amended the Collins Amendment with language clarifying that the Federal Reserve could promulgate capital rules for financial holding companies with insurance operations that differed from the capital rules put forth for banks. In addition, P.L. 113-279 specifically limited the

[38] *Metlife, Inc. v. Financial Stability Oversight Council*, Civil Action No. 15-45 (D. D.C. filed Jan 13, 2015); see also CRS Legal Sidebar WSLG1164, *MetLife's SIFI Designation Goes to Court*, by M. Maureen Murphy, CRS Legal Sidebar WSLG1554, *Trial Judge Scraps FSOC's MetLife SiFi Designation: Appeal to Follow*, by M. Maureen Murphy, and CRS Legal Sidebar WSLG1620, *FSOC Appeals District Court Rejection of Its MetLife SiFi Designation as "Profoundly Mistaken"*, by M. Maureen Murphy.

[39] Information on the FDIC's role in implementing Dodd-Frank can be found at http://www.fdic.gov/regulations/reform/.

[40] See, for example, U.S. Congress, Senate Committee on Banking, Housing, and Urban Affairs, Subcommittee on Financial Institutions and Consumer Protection, *Finding the Right Capital Regulations for Insurers*, 113th Cong., 2nd sess., March 11, 2014.

Federal Reserve's authority to require insurers to file financial statements using accounting standards other than those used by the state regulators.

Federal Reserve officials have indicated in various fora the understanding that insurers have a different composition of assets and liabilities than banks and that Federal Reserve oversight of insurers needs to be tailored to account for this.[41] Insurers, however, have expressed concern that Federal Reserve capital rules may not take account of particular characteristics of the industry and describe potential rules as "bank-centric."[42] Several insurers who previously operated under bank or thrift holding companies have sought to divest their depository subsidiaries to avoid Federal Reserve oversight and the resulting application of the various rules put forth in Dodd-Frank.[43] MetLife is the largest firm to divest its depository subsidiary, although such steps would not prevent the FSOC from designating an insurer as systemically important and thus subject to Federal Reserve oversight from this perspective. This is precisely what occurred with MetLife as the FSOC designated the company as systemically important on December 18, 2014.

The application of Section 619 of Dodd-Frank, commonly known as the "Volcker Rule," could also affect insurers with banking subsidiaries. This section includes restrictions on proprietary trading that potentially could constrain the investment strategies of insurers. The language, however, includes an exemption for trading done "by a regulated insurance company directly engaged in the business of insurance for the general account of the company by any affiliate of such regulated insurance company, provided that such activities by any affiliate are solely for the general account of the regulated insurance company."[44] The transactions must also comply with applicable law, regulation, or guidance. There must be no determination by the regulators that a relevant law, regulation, or guidance is insufficient to protect the safety and soundness of the banking entity or the financial stability of the United States.[45] The FSOC released a study on the Volcker Rule required by Dodd-Frank, which includes a discussion of the insurance company exemption with a particular recommendation that "the appropriate Agencies should carefully monitor fund flows between banking entities and insurance companies, to guard against 'gaming' the Volcker Rule."[46] The final Volcker Rule was published on December 13, 2013.[47]

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[41] See, for example, Testimony by Mark Van Der Weide, Deputy Director, Division of Banking Supervision and Regulation, Board of Governors of the Federal Reserve, before U.S. Congress, Senate Committee on Banking, Housing, and Urban Affairs, *The State of the Insurance Industry and Insurance Regulation*, 114th Cong., 1st sess., April 28, 2015, available at http://www.banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=f0a5b4ba-d6ab-41f0-a681-df896d744e38.

[42] Comments can be found at http://www.federalreserve.gov/apps/foia/ViewComments.aspx?doc_id=R-1442&doc_ver=1, see, for example, page 25 of the State Farm comment letter at http://www.federalreserve.gov/SECRS/2012/October/20121025/R-1442/R-1442_101912_109851_308150202515_1.pdf.

[43] See, for example, SNL Financial, "Another insurer-owned bank seeks shelter from oncoming regulatory storm," November 6, 2012, available at http://www.snl.com/InteractiveX/article.aspx?CDID=A-16216891-11568&KPLT=2.

[44] P.L. 111-203 §619(d)(1)(F).

[45] This description is from CRS Report R41298, *The "Volcker Rule": Proposals to Limit "Speculative" Proprietary Trading by Banks*, by David H. Carpenter and M. Maureen Murphy; please see this report and CRS Report R43440, *The Volcker Rule: A Legal Analysis*, by David H. Carpenter and M. Maureen Murphy.

[46] Financial Stability Oversight Council, *Study & Recommendations On Prohibitions On Proprietary Trading & Certain Relationships With Hedge Funds & Private Equity Funds*, January 2011, pp. 71-75.

[47] *Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds*, 79 Fed. Reg. 5,535 (January 31, 2014), available at http://www.gpo.gov/fdsys/pkg/FR-2014-01-31/pdf/2013-31511.pdf. The regulations were issued in a coordinated fashion, rather than issued jointly. As a result, there currently are some minor differences in the regulations issued by each federal regulator, and other differences may be implemented over time. For example, the Commodity Futures Trading Commission (CFTC) issued "substantively similar" regulations separately from the other financial regulators. 79 Fed, Reg. 5,808 (January 31,

The Federal Reserve issued an advance notice of proposed rulemaking (ANPR) regarding insurer capital standards on June 3, 2016. The ANPR comprised separate rules for insurers that are designated as SIFIs and those overseen by the Federal Reserve due to a depository subsidiary. Insurer SIFIs would be subject to a *consolidated approach* that would "categorize an entire insurance firm's assets and insurance liabilities into risk segments, apply appropriate risk factors to each segment at the consolidated level, and then set a minimum ratio of required capital." Non-SIFI insurers would be subject to a *building block approach* that would "aggregate existing capital requirements across a firm's different legal entities to arrive at a combined, group-level capital requirement." The capital levels resulting from the building block approach would, however, be subject to adjustment by the Federal Reserve.[48]

Surplus Lines and Reinsurance

Title V, Subtitle B of the Dodd-Frank Act, entitled the Nonadmitted and Reinsurance Reform Act of 2010 (NRRA), addresses a relatively narrow set of insurance regulatory issues pre-dating the financial crisis. In the area of nonadmitted (or *surplus lines*)[49] insurance, the act harmonizes, and in some cases reduces, regulation and taxation of this insurance by vesting the "home state" of the insured with the sole authority to regulate and to collect the taxes on a surplus lines transaction.[50] The taxes collected may be distributed according to a future interstate compact or agreement, but absent such an agreement their distribution would be within the authority of the home state. It also preempts any state laws on surplus lines eligibility that conflict with the NAIC model law unless the states include alternative uniform requirements as part of an agreement on taxes and implement "streamlined" federal standards allowing a commercial purchaser to access surplus lines insurance.[51] For reinsurance transactions, it vests the home state of the insurer purchasing the reinsurance with the authority over the transaction while vesting the home state of the reinsurer with the sole authority to regulate the solvency of the reinsurer.

NAIC and the National Conference of Insurance Legislators (NCOIL) both developed interstate agreements that, if adopted by the states, would allocate among the states the premium taxes paid to an insured's home state as permitted by the Dodd-Frank Act. The two models that were developed, however, differed significantly as to the extent of authority that would be ceded by the states to the new body overseeing the agreement. NCOIL's Surplus Lines Insurance Multistate Compliance Compact (SLIMPACT) is a broader agreement that would address surplus lines regulatory issues and taxes, whereas the NAIC's Nonadmitted Insurance Multi-State Agreement (NIMA) was more narrowly focused on tax allocation. Each approach was ratified by some states, but most states have ratified neither. This lack of uniformity was addressed in congressional hearings, and representatives of the NAIC and NCOIL particularly pledged to address the issue, possibly through some sort of blending of the two approaches, before the House Financial Services Committee in 2011.[52] Relatively few states joined either SLIMPACT or NIMA and

2014), available at http://www.gpo.gov/fdsys/pkg/FR-2014-01-31/pdf/2013-31476.pdf.

[48] Quotations from Federal Reserve Board of Governors, press release, June 3, 2016, at https://www.federalreserve.gov/newsevents/press/bcreg/20160603a.htm.

[49] Surplus lines insurance is insurance sold by insurance companies not licensed in the particular state where it is sold. For background on this insurance, see CRS Report RS22506, *Surplus Lines Insurance: Background and Current Legislation*, by Baird Webel.

[50] P.L. 111-203 §501.

[51] P.L. 111-203 §525.

[52] See U.S. Congress, House Committee on Financial Services, Subcommittee on Insurance, Housing and Community Opportunity, *Insurance Oversight: Policy Implications for U.S. Consumers, Businesses and Jobs*, 112th Cong., 1st sess.,

NIMA has since begun winding down operations.[53] In the absence of some form of agreement between states, the federal requirement for home state regulation and taxation remains in effect.

International Issues

Although financial services is not an industry that produces a tangible good to be shipped across borders, the trade in such services makes up a large segment of international trade. The United States has generally experienced a surplus in trade in financial services, other than insurance, but in insurance services the United States has consistently run a deficit with the rest of the world.[54] Consolidations in the insurance industry are creating larger international entities with growing market shares, particularly in the reinsurance market. Some have speculated that the growing "internationalization" of the financial services industry means governments may find it difficult to reform their regulation in isolation. The need for a single voice at the federal level to represent U.S. insurance interests on the international stage is a frequently heard argument for increased federal involvement in insurance regulation. The FIO is specifically tasked with developing federal policy in international insurance matters.

International Insurance Regulatory Standards

In response to the financial crisis of 2007-2009, the Group of 20 Heads of State established the Financial Stability Board (FSB) with a mandate to promote international financial stability. Primary U.S. members of the FSB are the Department of the Treasury, the Federal Reserve, and the Securities and Exchange Commission. The FSB coordinates with the International Association of Insurance Supervisors in establishing policies to address financial stability concerns within the insurance sphere. **Figure 1** shows a graphical representation of the international financial architecture relating to insurance.[55]

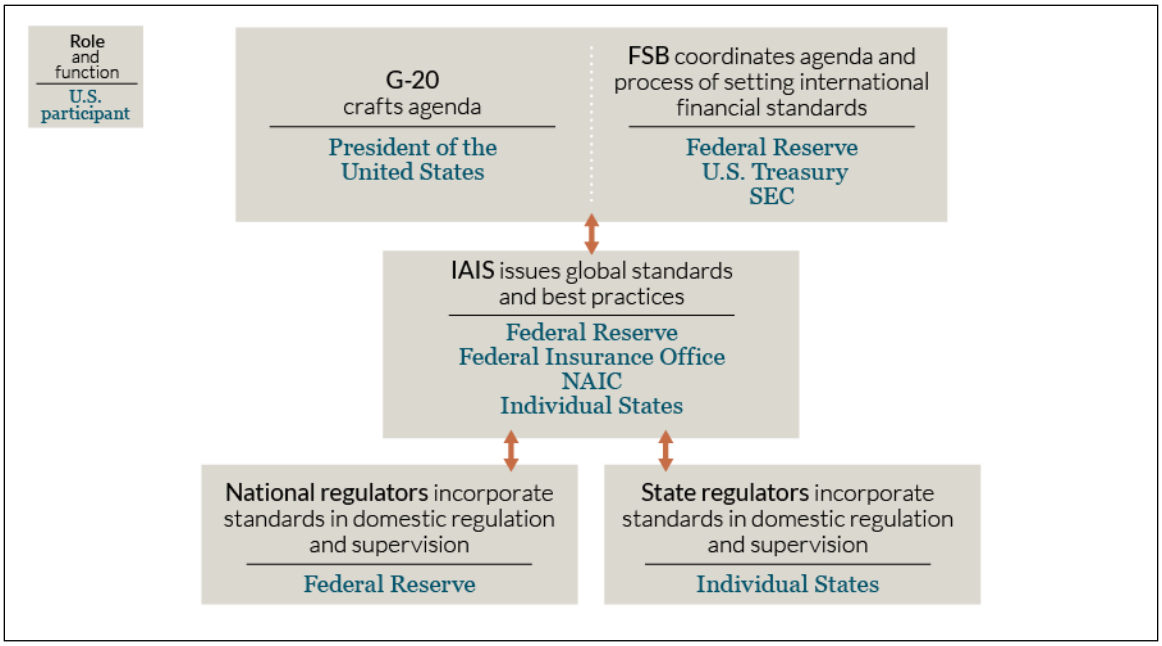
July 28, 2011, particularly the statements by Mr. Clay Jackson and Ms. Letha E. Heaton, available at http://financialservices.house.gov/Calendar/EventSingle.aspx?EventID=252895.

[53] See, for example, SNL Financial, "Surplus lines pact gains 2 states, but no boost to tax sharing," May 13, 2014; SNL Financial, "Louisiana to withdraw from national surplus lines agreement," July 15, 2015, and Non-Admitted Insurance Multi-State Association, Inc., "NIMA Board Votes to Dissolve," press release, May 2, 2016, at https://www.slai.org/info/2016-05-02_NimaDissolves.pdf.

[54] In 2015, U.S. exports of non-insurance financial services were $102.5 billion versus imports of $25.2 billion compared with insurance exports that totaled $17.1 billion versus imports of $47.8 billion. See the Bureau of Economic Analysis website at http://www.bea.gov/iTable/iTable.cfm?ReqID=62&step=1#reqid=62&step=6&isuri=1&6210=4&6200=160, Table 2.1.

[55] For a general overview of the international financial architecture, please see CRS In Focus IF10129, *Introduction to Financial Services: International Supervision*, by Martin A. Weiss.

Figure 1. International Financial Architecture for Insurance



Source: Congressional Research Service.

The IAIS, originally created in 1994, is made up primarily of insurance regulators from around the world with most jurisdictions having membership. Its mission is "to promote effective and globally consistent supervision of the insurance industry,"[56] including international standard setting and a variety of guidances and educational efforts. U.S. members include all the individual states, the NAIC, the Federal Reserve, and the U.S. Department of the Treasury's FIO. FIO and the Federal Reserve have only become IAIS members following passage of the Dodd-Frank Act.[57] The FIO director currently serves as chair of the IAIS Financial Stability and Technical Committee, which plays a central role in drafting standards proposed by the IAIS. The NAIC coordinates individual state participation in IAIS committees and working groups. According to the NAIC, three NAIC members serve on the IAIS Executive Committee, including one as vice chair. Three NAIC members serve on the Financial Stability and Technical Committee, including one as vice chair. State regulators and NAIC representatives also serve on many other working parties of the IAIS. The 56 members of the NAIC have 15 votes in the IAIS general meetings, with the NAIC designating which of its members may exercise their votes.[58]

The FSB, in consultation with the IAIS, has identified nine global systemically important insurers (G-SIIs), with three U.S. insurers among them (AIG, MetLife, and Prudential Financial). The IAIS is developing a general Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame)[59] as well as specific capital standards to apply to G-SIIs and

[56] From the International Association of Insurance Supervisors (IAIS) website at http://www.iaisweb.org/About-the-IAIS-28.

[57] P.L. 111-203.

[58] The 56 NAIC members include all 50 states plus U.S territories and the District of Columbia. The 15 votes and NAIC role are codified in the IAIS bylaws, Article 6(4)(b), available at http://iaisweb.org/index.cfm?event=openFile&nodeId=34510.

[59] For more information, see, IAIS, Frequently Asked Questions for The IAIS Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame), April 26, 2016, at http://www.iaisweb.org/page/supervisory-

additional standards intended for other IAIGs as requested by the FSB. The IAIS announced the plan for capital standards in 2013 and is currently in the second round of consultations, with comments closing in October 2016 and completion expected mid-2017.[60]

Any standards created by the IAIS are non-binding, and would not take full effect until adoption by the sovereign entities with legal authority for regulating insurance. In the United States, such authority is vested primarily with the individual states. This would mean that, in general, if individual state legislatures and regulators do not enact new laws or issue new regulations, international standards would not directly affect most insurers in the United States. It is possible as well that the Federal Reserve might implement some IAIS standards through its authority over SIFIs and holding companies with depository subsidiaries even if the states do not act. U.S. insurers operating outside of the United States also might be affected by IAIS standards imposed by regulators in other countries.

The international standard setting by the IAIS and the G-SII designations have raised concerns in Congress, particularly with regard to the effect these efforts might have on the competitiveness of U.S. insurers and possible weakening of the U.S. regulatory system. One particular point of difference between foreign and domestic insurance regulators is the degree of focus on individual insurance subsidiaries versus the overall financial institution. State regulators in the United States historically have taken the first approach, focusing on ensuring that individual insurance subsidiaries have sufficient capital to fulfill the promises inherent in the contracts the companies have made with policyholders. The capital standards being discussed currently at the IAIS focus more on the solvency of an overall insurance group, with some observers raising the possibility of transferring capital between subsidiaries to keep the group as a whole solvent. This approach could improve financial stability as a whole if it prevents a large insurer from becoming insolvent, but could also put individual policyholders at risk if there ends up not being enough capital to pay their claims. The NAIC has indicated specifically that "It is critical that the free flow of capital (i.e., assets) across a group should not jeopardize the financial strength of any insurer in the group."[61]

The European Union and Solvency II

The European Union (EU), the United States' biggest trading partner in insurance services, is implementing a comprehensive program to transform the EU into a single market for financial services. Part of this is an updated solvency regime for insurers—known as Solvency II—attempting to more closely match the capital required by regulators to the risks undertaken by insurers. The EU describes it as "an ambitious proposal that will completely overhaul the way we ensure the financial soundness of our insurers. We are setting a world-leading standard that requires insurers to focus on managing all the risks they face and enables them to operate much more efficiently."[62]

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material/common-framework/file/60333/comframe-frequently-asked-questions-updated-26-april-2016.

[60] IAIS, *Risk-based Global Insurance Capital Standard Version 1.0 Public Consultation Document*, July 19, 2016, at http://www.iaisweb.org/page/supervisory-material/insurance-capital-standard/file/61565/2016-risk-based-global-insurance-capital-standard-ics-consultation-document.

[61] National Association of Insurance Commissioners, *U.S. State Insurance Regulators' Views: International Capital Proposals*, December 2013, p. 2, available at http://www.naic.org/documents/committees_g_capital_position_statements.pdf.

[62] Charlie McCreevy, European Union Internal Market and Services Commissioner, quoted in "'Solvency II': EU to take global lead in insurance regulation" available at http://europa.eu/rapid/pressReleasesAction.do?reference=IP/07/1060&format=HTML&aged=0&language=EN&guiLanguage=en. The general EU website on Solvency II is

In some ways, Solvency II is purely an internal EU project designed to more closely harmonize laws among the EU countries. However, as part of the Solvency II project, new *equivalency* determinations of foreign jurisdictions are to be made by the EU.[63] An equivalency determination would allow insurers from a foreign jurisdiction to operate throughout the EU as do EU insurers. If the U.S. state-centered supervision of insurers is not judged to be "equivalent" to the EU insurance supervision, U.S. insurers may face more difficulty in operating in EU markets. There have been suggestions in the past that an EU regulatory change might serve as "a useful tool in international trade negotiations as it could help improve access for European reinsurers to foreign markets," such as the United States.[64] A June 6, 2014, letter from the European Commission to FIO and the NAIC drew an explicit connection between an equivalency designation applying to the United States and the U.S. removal of reinsurance capital requirements that the states place on non-U.S. reinsurers.[65]

Solvency II came into effect in the EU at the beginning of 2016. The EU has granted provisional equivalence to the United States along with five other countries and full equivalence to two countries. The grant of provisional U.S. equivalence, however, applies only to capital requirements of EU insurers with U.S. operations[66] and U.S. insurers have begun experiencing difficulties operating in EU countries.[67]

Reinsurance Collateral

Reinsurance collateral refers to U.S. state regulatory requirements that reinsurance issued by non-U.S. or *alien* reinsurers must be backed by collateral deposited in the United States. [68] In the past, this requirement generally was for a 100% collateral deposit. Non-U.S. reinsurers long resisted this requirement, pointing out, among other arguments, that U.S. reinsurers do not have any collateral requirements in many foreign countries and that the current regulations do not recognize when an alien reinsurer cedes some of the risk back to a U.S. reinsurer. In the past, the National Association of Insurance Commissioners (NAIC) and the individual states declined to reduce collateral requirements, citing fears of unpaid claims from non-U.S. reinsurers and an inability to collect judgments in courts overseas. This stance, however, has changed in recent years.

In 2009, the NAIC put forth draft federal legislation to create a board with the power to enforce national standards for reinsurance collateral, including the reduction of collateral for highly rated reinsurers.[69] In 2010, an NAIC Task Force approved recommendations to reduce required

http://ec.europa.eu/internal_market/insurance/solvency/index_en.htm.

[63] For an explanation of the criteria see EIOPA website, *Equivalence*, at https://eiopa.europa.eu/external-relations/equivalence.

[64] European Commission, "Commission Proposes a Directive to Create a Real EU-Wide Market for Reinsurance," *Internal Market: Financial Services: Insurance: Press Release*, April 21, 2004, at http://europa.eu/rapid/pressReleasesAction.do?reference=IP/04/513&format=PDF&aged=1&language=EN&guiLanguage=en.

[65] Letter from Jonathan Faull, director general, Internal Market and Services, European Commission, to Michael McRaith, director, Federal Insurance Office, and Benjamin Nelson, chief executive officer, NAIC, June 6, 2014.

[66] See European Commission, *Equivalence Decisions*, at http://ec.europa.eu/finance/insurance/solvency/international/index_en.htm.

[67] See, for example, Elizabeth Festa, "Insurers, reinsurers voice strong concern over growing costs, burdens of Solvency II," *SNL Financial*, August 29, 2016.

[68] In the United States, the term *foreign* insurer generally denotes an insurer that is chartered in a different state; those insurers from a different country have been called *alien* insurers.

[69] NAIC, "Naic Proposes Reinsurance Regulatory Modernization Act Of 2009," press release, September 23, 2009, at

collateral based on the financial strength of the reinsurer involved and recognition of the insurer's domiciliary regulator as a qualified jurisdiction. This proposal was adopted as a model law and accompanying model regulation by the NAIC in November 2011.[70] To take effect, however, these changes must be made to state law and regulation by the individual state legislatures and insurance regulators.

According to the NAIC, as of April 1, 2016, 32 jurisdictions have adopted the model law with 22 also adopting the model regulation, representing approximately 66% of total premiums.[71] To date, more than 30 reinsurers have been approved by the states as certified reinsurers for reduction in collateral requirements. The NAIC's Reinsurance Financial Analysis Working Group has conducted peer reviews for more than 30 certifications issued thus far by various states, and has developed a process for certified reinsurers to be approved in multiple states on a streamlined basis (known as *passporting*). To receive the reduced collateral requirements, the reinsurer's home jurisdiction must also be reviewed and listed on the NAIC List of Qualified Jurisdictions. As of January, 2015, seven jurisdictions have been approved.[72]

The state actions addressing reinsurance collateral requirements, however, have not fully met concerns regarding the issue. Non-U.S. reinsurers reportedly would like a single standard across the United States that would eliminate, not just reduce, collateral requirements[73] and this desire is a significant part of the EU's expressed motivation to enter into covered agreement negotiations. A representative of the Council of the EU indicated that "an agreement with the US will greatly facilitate trade in reinsurance and related activities" and would "enable us, for instance, to recognise each other's prudential rules and help supervisors exchange information."[74]

State Regulatory Modernization Efforts

Following the passage of GLBA, state insurance regulators working through the NAIC embarked on a regulatory modernization program. These efforts were in response to both the mounting criticisms of state insurance regulation and the recognition of the growing convergence of financial services and financial services products. In early 2000, NAIC members signed a *Statement of Intent: The Future of Insurance Regulation*, in which they pledged "to modernize insurance regulation to meet the realities of the new financial services marketplace." New NAIC working groups were formed addressing issues such as state privacy protections, reciprocity of state producer licensing laws, promotion of "speed to market" of new insurance products, development of state-based uniform standards for policy form filings, and other proposed improvements to state rate and form filing requirements. Highlights of the post-GLBA NAIC efforts include the following:

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http://www.naic.org/Releases/2009_docs/2009_reinsurance_regulatory_modernization.htm.

[70] NAIC, *Credit for Reinsurance Model Law* (#785) and NAIC, *Credit for Reinsurance Model Regulation* (#786).

[71] NAIC, *Reinsurance*, April 7, 2016, at http://www.naic.org/cipr_topics/topic_reinsurance.htm.

[72] The seven jurisdictions are: Bermuda – Bermuda Monetary Authority (BMA); France – Autorité de Contrôle Prudentiel et de Résolution (ACPR); Germany – Federal Financial Supervisory Authority (BaFin); Ireland – Central Bank of Ireland; Japan – Financial Services Agency (FSA); Switzerland – Financial Market Supervisory Authority (FINMA); and United Kingdom – Prudential Regulation Authority of the Bank of England (PRA), see NAIC, *List of Qualified Jurisdictions*, at http://www.naic.org/documents/committees_e_reinsurance_qualified_jurisdictions_list.pdf.

[73] See, for example, Reuters, "EU Mounts Fresh Bid to End U.S. Reinsurance Collateral Rule," April, 21, 2015, available at http://www.reuters.com/article/2015/04/21/eu-usa-insurance-idUSL5N0XI44T20150421.

[74] Council of the European Union, "EU-US agreement on reinsurance: Council agrees to negotiations," press release, April 21, 2015, http://www.consilium.europa.eu/en/press/press-releases/2015/04/21-eu-us-agreement-reinsurance.

- Certification of 42 states (as of February 2008) as reciprocal jurisdictions for producer licensing laws,[75] thus exceeding the GLBA requirements to prevent the establishment of NARAB. As discussed above, however, the 114th Congress ultimately acted to create a NARAB despite the state efforts.
- Growth of the System for Electronic Rate and Form Filing (SERFF), intended to be a single, one-stop point of entry for insurers to file changes to rates and forms. More than 637,000 filings were made through the system in 2015, up from about 3,700 in 2001, and 49 states participate in the system.[76]
- State approvals of the Interstate Insurance Product Regulation Compact. This compact is intended to provide increased regulatory uniformity and a single point of product filing for four insurance lines—life, annuities, disability income, and long-term care. It came into effect in May 2006.[77] Currently, 43 states[78] representing over 70% of the insurance premium volume have joined the compact.

The NAIC maintains that states are better positioned than the federal government to serve the interests of U.S. insurance consumers, emphasizing that state regulators are better suited to ensure that consumer interests are not lost in the arena of commercial competition. In 2015, according to the NAIC, the total budget for the state insurance departments was $1.36 billion. The states handled nearly 300,000 official consumer complaints and nearly 1.9 million consumer inquiries regarding their policies and their treatment by insurance companies and agents. The states collectively employed more than 11,300 employees to handle these complaints and perform the other functions of the state insurance departments.[79]

Since the financial crisis, the NAIC has undertaken another round of regulatory changes. Three initiatives specifically identified by the NAIC are

- *Holding company oversight reform*. Historically, insurer oversight has focused on the individual legal entities and subsidiaries, but the financial crisis brought greater scrutiny on holding company and overall insurer group issues. In response, the NAIC adopted the revisions to model laws and regulations relating to holding company oversight.[80] The revisions included

  > expanded ability to evaluate any entity within an insurance holding company system; enhancements to the regulator's rights to access books and records and compelling production of information; establishment of expectation of funding with regard to regulator participation in supervisory colleges; and enhancements in corporate governance, such as Board of Directors and Senior Management responsibilities.[81]

[75] NAIC, *Producer Licensing Assessment Aggregate Report Of Findings*, February 7, 2018, at http://www.naic.org/documents/committees_ex_pltf_plwg_PLC_assessment_aggregate_report.pdf.

[76] See NAIC, *About SERFF*, at http://www.serff.org/about.htm.

[77] See Interstate Insurance Product Regulation Commission website, *About the IIPRC*, at http://www.insurancecompact.org/about.htm.

[78] Puerto Rico is also a member.

[79] Statistics from NAIC, *2015 Insurance Department Resources Report, part 1*, at http://www.naic.org/prod_serv/STA-BB-16-01.pdf.

[80] Specifically the Insurance Holding Company System Regulatory Act (Model #440) and the Insurance Holding Company System Model Regulation with Reporting Forms and Instructions (Model #450).

[81] See NAIC, *Group Supervision*, October 24, 2016, at http://www.naic.org/cipr_topics/topic_group_supervision.htm.

The NAIC reports all 50 states, the District of Columbia, and Puerto Rico have adopted these changes.

- *Enterprise risk management*. As part of insurer solvency oversight, emphasis both internationally and in the United States has been placed on companies themselves assessing, and reporting, the risks they are taking. This is generally accomplished through an "Own Risk and Solvency Assessment" (ORSA). An ORSA requires insurers to "issue their own assessment of their current and future risk through an internal risk self-assessment process and it will allow regulators to form an enhanced view of an insurer's ability to withstand financial stress."[82] In September 2012, the NAIC adopted a model law[83] that would require an annual ORSA and has produced a guidance manual on the topic. The NAIC reports that 40 states have passed the ORSA legislation.
- *Principle-based reserving (PBR)*.[84] State requirements for life insurance reserves have remained static for decades, while insurance products themselves have increased in complexity. In response, the NAIC created, and states have begun adopting, a revised model law[85] to transition life insurance reserving to a principle-based approach, from the current formulaic approach. According to the NAIC as of December 1, 2016, 46 states comprising 85.7% of premiums have enacted PBR legislation. To avoid market disruption or an un-level playing field, PBR had not become operational until 42 states comprising at least 75% of the U.S. market approved the law. With these thresholds past, PBR will begin being applied in 2017.

[82] See NAIC, *Own Risk and Solvency Assessment*, July 5, 2016, http://www.naic.org/cipr_topics/topic_own_risk_solvency_assessment.htm.

[83] The Risk Management and Own Risk and Solvency Assessment Model Act (#505).

[84] See NAIC, *Principle-Based Reserving*, December 8, 2016, at http://www.naic.org/cipr_topics/principle_based_reserving_pbr.htm.

[85] The Standard Valuation Law (#820).

Appendix A. Evolution of Insurance Regulation Through the 111th Congress

Insurance companies, unlike banks and securities firms, have been chartered and regulated solely by the states for the past 150 years. One important reason for this is an 1868 U.S. Supreme Court decision.[86] In *Paul v. Virginia*, the Court held that the issuance of an insurance policy was not a transaction occurring in interstate commerce and thus not subject to regulation by the federal government under the Commerce Clause of the U.S. Constitution. Courts followed that precedent for the next 75 years. In a 1944 decision, *U.S. v. South-Eastern Underwriters Association*, the Court found that the federal antitrust laws were applicable to an insurance association's interstate activities in restraint of trade.[87] Although the 1944 Court did not specifically overrule its prior holding in *Paul*, *South-Eastern Underwriters* created significant apprehension about the continued viability of state insurance regulation and taxation of insurance premiums. By 1944, the state insurance regulatory structure was well established, and a joint effort by state regulators and insurance industry leaders to legislatively overturn the *South-Eastern Underwriters* decision led to the passage of the McCarran-Ferguson Act of 1945.[88] The act's primary purpose was to preserve the states' authority to regulate and tax insurance.[89] The act also granted a federal antitrust exemption to the insurance industry for "the business of insurance."[90]

After 1945, the jurisdictional stewardship entrusted to the states under McCarran-Ferguson was reviewed by Congress on various occasions. Some narrow exceptions to the 50-state structure of insurance regulation have been enacted, such as one for some types of liability insurance in the Liability Risk Retention Act created by Congress in 1981 and amended in 1986.[91] In general, however, when proposals were made in the past[92] to transfer insurance regulatory authority to the federal government, they were successfully opposed by the states as well as by a united insurance industry. Such proposals for increased federal involvement usually spurred a series of regulatory reform efforts at the individual state level and by state groups, such as the National Association of Insurance Commissioners (NAIC) and the National Conference of Insurance Legislators (NCOIL). Such efforts were directed at correcting perceived deficiencies in state regulation and forestalling federal involvement. They were generally accompanied by pledges from state regulators to work for more uniformity and efficiency in the state regulatory process.

A major effort to transfer insurance regulatory authority to the federal government began in the mid-1980s and was spurred by the insolvencies of several large insurance companies. Former

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[86] *Paul v. Virginia*, 75 U.S. (8 Wall.) 168 (1868).

[87] *U.S. v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944).

[88] 15 U.S.C. §1011 *et seq*.

[89] Richard Cordero, *Exemption or Immunity from Federal Antitrust Liability Under McCarran-Ferguson (15 U.S.C. 1011-1013) and State Action and Noer-Pennington Doctrines for Business of Insurance and Persons Engaged in It*, 116 ALR Fed 163, 194 (1993).

[90] 15 U.S.C. §1012(b). The Supreme Court has made clear that the business of insurance does not include all business of insurers in *Group Health and Life Insurance, Co. v. Royal Drug, Co.*, 440 U.S. 205, 279 (1979). For further explanation of this distinction, see the CRS Report RL33683, *Courts Narrow McCarran-Ferguson Antitrust Exemption for "Business of Insurance": Viability of "State Action" Doctrine as an Alternative*, by Janice E. Rubin.

[91] 15 U.S.C. §3901 *et seq*. See CRS Report RL32176, *The Liability Risk Retention Act: Background, Issues, and Current Legislation*, by Baird Webel.

[92] Most such proposals prior to the 1990s focused on relatively narrow amendments to McCarran-Ferguson rather than large-scale replacement of the state regulatory system.

House Energy and Commerce Committee Chairman John Dingell, whose committee had jurisdiction over insurance at the time, questioned whether state regulation was up to the task of overseeing such a large and diversified industry. He chaired several hearings on the state regulatory structure and also proposed legislation that would have created a federal insurance regulatory agency modeled on the Securities and Exchange Commission (SEC). State insurance regulators and the insurance industry opposed this approach and worked together to implement a series of reforms at the state level and at the NAIC. Among the reforms implemented was a new state accreditation program setting baseline standards for state solvency regulation. Under the accreditation standards, to obtain and retain its accreditation, each state must have adequate statutory and administrative authority to regulate an insurer's corporate and financial affairs and the necessary resources to carry out that authority. In spite of these changes, however, another breach in the state regulatory system occurred in the late 1990s. Martin Frankel, an individual who had previously been barred from securities dealing by the SEC, slipped through the oversight of several states' insurance regulators and diverted more than $200 million in premiums and assets from a number of small life insurance companies into overseas accounts.[93]

Another state reform largely implemented in the late 1980s and early 1990s was the introduction of state insurance guaranty funds.[94] These funds, somewhat analogous in function to the Federal Deposit Insurance Corporation (FDIC) for banks, provide protection for insurance consumers who hold policies from failed insurance companies. If an insurance company is judged by a state insurance regulator to be insolvent and unable to fulfill its commitments, the state steps in to rehabilitate or liquidate the insurer's assets. The guaranty fund then uses the assets to pay the claims on the company, typically up to a limit of $300,000 for property/casualty insurance[95] and $300,000 for life insurance death benefits and $100,000 for life insurance cash value and annuities.[96] In most states, the existing insurers in the state are assessed to make up the difference should the company's assets be unable to fund the guaranty fund payments. This after the fact assessment stands in contrast to the FDIC, which is funded by assessments on banks prior to a bank failure and which holds those assessments in a segregated fund until needed. Insurers who are assessed by guaranty funds generally are permitted to write off the assessments on future state taxes, which indirectly provide state support for the guaranty funds.

The Gramm-Leach-Bliley Act

The 1999 Gramm-Leach-Bliley Act (GLBA)[97] significantly overhauled the general financial regulatory system in the United States. Support for GLBA came largely as a result of market developments frequently referred to as *convergence*. Convergence in the financial services context refers to the breakdown of distinctions separating different types of financial products and services, as well as the providers of once separate products. Drivers of such convergence include globalization, new technology, e-commerce, deregulation, market liberalization, increased

[93] See, for example, "17-Year Sentence Affirmed for Investor Who Looted Insurers," *New York Times*, March 24, 2006, available at http://www.nytimes.com/2006/03/24frankel..html?ref=martinfrankel.

[94] For more information see CRS Report RL32175, *Insurance Guaranty Funds*, by Baird Webel.

[95] National Conference of Insurance Guaranty Funds, "Facts and Statistics," available at http://www.ncigf.org/media-facts.

[96] National Organization of Life & Health Insurance Guaranty Associations, "Frequently Asked Questions," available at http://www.nolhga.com/policyholderinfo/main.cfm/location/questions.

[97] P.L. 106-102, 113 Stat. 1338.

competition, tighter profit margins, and the growing number of financially sophisticated consumers.

GLBA intended to repeal federal laws that were inconsistent with the way that financial services products were actually being delivered, and it removed many barriers that kept banks or securities firms from competing with, or affiliating with, insurance companies. The result was the creation of a new competitive paradigm in which insurance companies found themselves in direct competition with brokerages, mutual funds, and commercial banks. GLBA did not, however, change the basic regulatory structure for insurance or other financial products. Instead, it reaffirmed the McCarran-Ferguson Act, recognizing state insurance regulators as the "functional" regulators of insurance products and those who sell them.[98]

Some insurance companies believe that in the post-GLBA environment, state regulation places them at a competitive disadvantage in the marketplace. They maintain that their non-insurer competitors in certain lines of products have federally based systems of regulation that are more efficient, while insurers remain subject to perceived inefficiencies of state insurance regulation, such as the regulation of rates and forms as well as other delays in getting their products to market. For example, life insurers with products aimed at retirement and asset accumulation must now compete with similar bank products. Banks can roll out such new products nationwide in a matter of weeks, while some insurers maintain that it can take as long as two years to obtain all of the necessary state approvals for a similar national insurance product launch. In the aftermath of GLBA, the largely united industry resistance to federal intervention in insurance changed. Many industry participants, particularly life insurers, larger property/casualty insurers, and larger insurance brokers, began supporting broad regulatory change for insurance in the form of an optional federal charter for insurance patterned after the dual chartering system for banks.[99]

GLBA also addressed the issue of modernizing state laws dealing with the licensing of insurance agents and brokers and made provision for a federally backed licensing association, the National Association of Registered Agents and Brokers (NARAB). NARAB would have come into existence three years after the date of GLBA's enactment if a majority of the states failed to enact the necessary legislation for uniformity or reciprocity at the individual state level. The requisite number of states enacted this legislation within the three-year period, and thus the NARAB provisions never came into effect. The issue of insurance producer licensing reciprocity or uniformity continued, as some saw and continue to see problems in the actions taken by the individual states. Not every state has passed legislation implementing reciprocity, and some have argued that it has not always been implemented as smoothly as desired even in those states that did.[100]

Insurance After the Gramm-Leach-Bliley Act

Congress passed the Gramm-Leach-Bliley Act to enhance competition among financial services providers. Though many observers expected banks, securities firms, and insurers to converge as

[98] Functional regulation would entail, for example, insurance regulators overseeing insurance products being offered by banks, while banking regulators would oversee banking products offered by insurers. Institutional regulation tends to focus on the charter of the institution; for example, banking regulators oversee all the activities of a bank even if the bank is offering insurance products.

[99] Banking charters are available from both the individual states and the federal government. For more information on optional federal charter legislation, see CRS Report RL34286, *Insurance Regulation: Federal Charter Legislation*, by Baird Webel.

[100] See, for example, the April 16, 2008, testimony by Tom Minkler on behalf of the Independent Insurance Agents and Brokers made before the House Financial Services Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises at http://www.house.gov/apps/list/hearing/financialsvcs_dem/minkler041608.pdf.

institutions after it passed, this has not occurred as expected. In fact, the major merger between a large bank, Citibank, and a large insurer, Travelers, which partially motivated the passage of GLBA, has effectively been undone. The corporation that resulted from the merger, Citigroup, has divested itself of almost all of its insurance subsidiaries. Although large bank-insurer mergers did not occur as expected, significant convergence continued. Instead of merging across sectoral lines, banks began distributing—but not "manufacturing"—insurance, and insurers began creating products that closely resembled savings or investment vehicles. Consolidation also continued within each sector, as banks merged with banks and insurers with insurers. In addition, although Congress instituted functional regulation in GLBA, regulation since has still tended to track institutional lines.

From the 107th through the 110th Congresses, congressional interest in insurance regulatory issues continued. A number of broad proposals for some form of federal chartering or other federal intervention in insurance regulation were put forward in both houses of Congress and by the Administration, but none were marked up or reported by the various committees of jurisdiction.[101] In the same time frame, a number of narrower bills affecting different facets of insurance regulation and regulatory requirements were also introduced in Congress, including bills addressing surplus lines and reinsurance, insurance producer licensing, and expansion of the Liability Risk Retention Act beyond liability insurance.

Insurance and the Financial Crisis

As the 110th Congress approached its close, the financial crisis that began in 2007 reached panic proportions with the conservatorship of Fannie Mae and Freddie Mac, the failure of Lehman Brothers, and the government rescue of American International Group (AIG) in September 2008. This crisis overlaid a range of new issues and arguments to the previously existing debate on insurance regulatory reforms. The financial crisis grew largely from sectors of the financial industry that had previously been perceived as presenting little systemic risk, including insurers. Some saw the crisis as resulting from failures or holes in the financial regulatory structure, particularly a lack of oversight for the system as a whole and a lack of coordinated oversight for the largest actors in the system. Those holding this perspective increased the urgency in calls for overall regulatory changes, such as the implementation of increased systemic risk regulation and federal oversight of insurance, particularly larger insurance firms. The generally good performance of insurers in the crisis, however, also provided additional affirmation to those seeking to retain the state-based insurance system.

Although insurers in general are considered to have weathered the financial crisis reasonably well, the insurance industry saw two notable failures—one general and one specific. The first failure was spread across the financial guarantee or monoline bond insurers. Before the crisis, there were about a dozen bond insurers in total, with four large companies dominating the business. This type of insurance originated in the 1970s to cover municipal bonds, but the insurers expanded their businesses since the 1990s to include significant amounts of mortgage-backed securities. In late 2007 and early 2008, strains began to appear due to this exposure to mortgage-backed securities. Ultimately some bond insurers failed and others saw their previously

[101] Broad proposals from the 107th to 110th Congresses included the National Insurance Act of 2007 (S. 40 and H.R. 3200, 110th Congress); the National Insurance Act of 2006 (S. 2509 and H.R. 6225, 109th Congress); the Insurance Consumer Protection Act of 2003 (S. 1373, 108th Congress); and the Insurance Industry Modernization and Consumer Protection Act (H.R. 3766, 107th Congress), and the 2008 *Blueprint for a Modernized Financial Regulatory Structure* released by the U.S. Department of the Treasury and available at http://www.treasury.gov/press-center/press-releases/Documents/Blueprint.pdf.

triple-A ratings cut significantly. These downgrades rippled throughout the municipal bond markets, causing unexpected difficulties for both individual investors and municipalities who might have thought they were relatively insulated from problems stemming from rising mortgage defaults.

The second failure in the insurance industry was that of a specific company, American International Group.[102] AIG had been a global giant of the industry, but it essentially failed in mid-September 2008. To prevent bankruptcy in September and October 2008, AIG sought more than $100 billion in assistance from the Federal Reserve, which received both interest payments and warrants for 79.9% of the equity in the company in return. Multiple restructurings of the assistance followed, including nearly $70 billion through the U.S. Department of the Treasury's Troubled Asset Relief Program (TARP). The rescue ultimately resulted in the U.S. government owning 92% of the company. The assistance for AIG has ended with all the Federal Reserve assistance repaid and the U.S. Department of the Treasury's sale of all of its equity stake in the company.

The near collapse of the bond insurers and AIG could be construed as regulatory failures. One of the responsibilities of an insurance regulator is to make sure the insurer remains solvent and is able to pay its claims. Because the states are the primary insurance regulators, some may go further and argue that these cases specifically demonstrate the need for increased federal involvement in insurance. The case of AIG, however, is a complicated one. Although AIG was primarily made up of state-chartered insurance subsidiaries, at the holding company level it was a federally regulated thrift holding company with oversight by the Office of Thrift Supervision (OTS). The immediate losses that caused AIG's failure came from both derivatives operations overseen by OTS and from securities lending operations that originated with securities from state-chartered insurance companies.

The 111th Congress responded to the financial crisis with the Dodd-Frank Wall Street Reform and Consumer Protection Act,[103] which enacted broad financial regulatory reform as detailed above. Attention on insurance regulation in the 112th and 113th Congresses was largely occupied with follow-up to the Dodd-Frank Act. The Dodd-Frank Act left many of the specifics up to regulatory rulemaking, and this rulemaking is still ongoing. Of particular concern was the specific approach that the Federal Reserve may take to bank or thrift holding companies who are primarily involved in insurance and the possibility of Financial Stability Oversight Council (FSOC) designating some insurers as systemically important and thus subject to additional oversight.

[102] See CRS Report R42953, *Government Assistance for AIG: Summary and Cost*, by Baird Webel.

[103] P.L. 111-203, 124 Stat. 1376. See CRS Report R41350, *The Dodd-Frank Wall Street Reform and Consumer Protection Act: Background and Summary*, coordinated by Baird Webel.

Appendix B. Constitutional Authority for Federal Regulation of the Business of Insurance[104]

Pursuant to the Commerce Clause of the U.S. Constitution,[105] it is generally constitutional for the federal government to regulate the business of insurance because, according to relevant Supreme Court precedent and subsequent decisions explaining the controlling case, the business of insurance is commerce.[106] It therefore may be regulated by the federal government in a manner coextensive with Congress's constitutional authority to regulate any other economic activity with international and interstate aspects.[107]

The authority of the federal government to regulate the business of insurance as interstate commerce was not always clear. The Supreme Court in *Paul v. Virginia* had previously held that "[issuing] a policy of insurance is not a transaction of interstate commerce."[108] The case challenged the constitutionality of a Virginia law that made it more difficult for insurance companies incorporated outside of Virginia to do business within the commonwealth. The insurance industry argued that the statute violated the dormant commerce clause, a legal concept rooted in the Commerce Clause of the Constitution, which prohibits states from discriminating against *foreign* (out-of-state) corporations.[109] The Court found that the Virginia law could not violate the Commerce Clause because insurance was not commerce. In making this determination, the Court appeared to rely on a rather narrow and mechanical definition of commerce.

> These contracts are not articles of commerce in any proper meaning of the word. They are not subjects of trade and barter offered in the market as something having an existence and value independent of the parties to them.... They are not commodities to be shipped or forwarded from one State to another.... They are like other personal contracts between parties which are completed by their signature and transfer of consideration. Such contracts are not inter-state transactions, though the parties may be domiciled in different States.[110]

Subsequent Supreme Court decisions affirmed the holding in *Paul* that the business of insurance was not commerce, and states relied upon this interpretation as they built regulatory systems for the business of insurance.[111]

Seventy-five years after *Paul*, in *United States v. South-Eastern Underwriters Associations*, the Supreme Court ruled differently, holding that the business of insurance is, in fact, commerce and

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[104] This appendix authored by CRS Legislative Attorney Kathleen Ruane.

[105] U.S. Const., Art. I, §8, cl. 3. ("The Congress shall have Power ... To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."). For a general discussion of Congress's Commerce Clause Powers, see CRS Report RL32844, *The Power to Regulate Commerce: Limits on Congressional Power*, by Kenneth R. Thomas.

[106] *United States v. South-Eastern Underwriters Assoc*., 322 U.S. 533 (1944).

[107] Id.

[108] 75 U.S. 168, 183 (1869).

[109] *Okla. Tax Comm'n v. Jefferson Lines*, 514 U.S. 175, 180 (1995) (The dormant commerce clause "prevent[s] a State from retreating into economic isolation or jeopardizing the welfare of the Nation as a whole, as it would do if it were free to place burdens on the flow of commerce across its borders that commerce wholly within those borders would not bear.")

[110] *Paul v. Virginia*, 75 U.S. at 183.

[111] See, e.g., *Hooper v. California*, 155 U.S. 648 (1895) ("The business of insurance is not commerce."); *New York Life Ins. Co. v. Deer Lodge County*, 231 U.S. 495 (1913) ("Contracts of insurance are not commerce.").

its interstate characteristics may be subject to federal regulation.[112] The case, while not explicitly overruling *Paul v. Virginia*, abrogated the *Paul* decision considerably.[113] *South-Eastern Underwriters* presented the Supreme Court squarely with the question of whether Congress had the power to directly regulate the insurance industry for the first time.[114] In the case, the Department of Justice had brought suit against certain insurance companies for violations of the Sherman Antitrust Act. The insurance companies that were accused of violating the antitrust laws argued that because the business of insurance was not interstate commerce, the Sherman Antitrust Act did not apply to the activities of the companies.

In deciding that the business of insurance is commerce and that it is also *interstate* commerce to which the federal antitrust laws did apply, the majority of the Court took a more practical and less mechanical view of commerce, generally, and the insurance industry, in particular, than the Court in *Paul*. The *South-Eastern Underwriters* Court began by describing the enormity of the insurance business as a portion of the U.S. economy and noted that many insurance companies operated out of the northeastern region of the country, but did business in multiple states, lending credence to the argument that insurance was, indeed, an interstate commercial enterprise.[115] Furthermore, since the *Paul* decision, other Supreme Court cases had made clear that intangible items, such as contracts not unlike insurance contracts, are items of commerce that can be regulated by Congress.[116] While the Court was willing to concede that "a contract of insurance, considered as a thing apart from negotiation and execution, does not itself constitute *interstate* commerce," the Court found, nonetheless, that "a nationwide business is not deprived of its interstate character merely because it is built upon sales contracts which are local in nature. Were the rule otherwise, few businesses could be said to be engaged in interstate commerce."[117]

The Court concluded its analysis of the Commerce Clause question with a strong endorsement of a broad reading of the powers of Congress to regulate the business of insurance as interstate commerce. "No commercial enterprise of any kind which conducts its activities across state lines has been held to be wholly beyond the regulatory power of Congress under the Commerce Clause. We cannot make an exception of the business of insurance."[118]

Shortly after the decision was issued in *South-Eastern Underwriters*, Congress passed the McCarran Ferguson Act[119] as a direct response to that decision. The first section of the act explicitly declares it to be the policy of the United States "that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence

[112] 322 U.S. 533 (1944).

[113] It appears that *South-Eastern Underwriters* did not explicitly overrule *Paul v. Virginia* because *Paul v. Virginia* presented a question regarding the limits of state authority under the commerce clause; whereas *South-Eastern Underwriters* presented a question regarding the authority of Congress to regulate the business of insurance as interstate commerce. 322 U.S. at 544.

[114] Id.

[115] Id. at 539-543.

[116] Id. at 546.

[117] Id. at 547.

[118] Id. at 553. It is worth noting that the decision in *South-Eastern Underwriters* was not a unanimous one. The case was decided 4-3. However, two of the dissenting Justices in the case explicitly agreed with the majority that Congress could regulate the insurance industry to the same extent that it could regulate other industries in interstate commerce. Id. at 562-63 (J.Stone, dissenting); Id. at 583 (J. Frankfurter, dissenting). Justices Frankfurter and Stone dissented from the majority because they found that the Sherman Antitrust Act, the law that the companies were accused of violating, was not intended to be applied to the insurance industry.

[119] Codified at 15 U.S.C. §1011 *et seq*.

on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States."[120] The act goes on to ensure state regulatory authority over the business of insurance by preventing federal preemption of state insurance regulations, with some notable exceptions. Specifically, McCarran Ferguson says that "[no] act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, *unless such Act specifically relates to the business of insurance*."[121]

Based upon the emphasized language, it appears that, even within McCarran-Ferguson, Congress has reserved for itself the right to directly regulate the business of insurance when appropriate. And the Supreme Court has upheld Congress's authority to do so. For example, in *Barnett Bank of Marion County v. Nelson*, the Supreme Court held that a federal law granting national banks the ability to sell insurance preempted a Florida statute that forbid banks from selling insurance.[122] The Court reviewed whether McCarran-Ferguson prevented the Florida statute from being superseded by the federal law, and found that because the federal law specifically related to the business of insurance, McCarran-Ferguson's provision preventing state insurance law preemption by federal statute did not apply. In this way, the Supreme Court upheld a federal regulation of the business of insurance, affirming that the business of insurance is commerce under the Constitution, and its interstate aspects may be regulated by Congress.

Congress's authority to regulate the business of insurance under the Commerce Clause extends only so far as Congress's authority to regulate interstate commerce. In the Patient Protection and Affordable Care Act,[123] Congress enacted a requirement for all U.S. citizens to purchase health insurance, commonly known as the *individual mandate*.[124] The requirement was challenged by a number of states as an unconstitutional exercise of Congress's powers to regulate interstate commerce. The Supreme Court agreed that the individual mandate was not a valid exercise of Congress's Commerce Clause power in a 2011 decision.[125] In his controlling opinion, Chief Justice Roberts held that while the Commerce Clause granted Congress broad authority to regulate economic activity, it did not grant Congress the power to compel individuals to engage in economic activity.[126] Therefore, though the Chief Justice found that Congress did not have the authority to impose the individual mandate under the Commerce Clause, Chief Justice Roberts ruled in this manner not because Congress does not have the power to regulate the business of insurance, but because the Commerce Clause does not grant Congress the authority to compel individuals to participate in economic activity.[127] While the individual mandate was ruled not to be a valid exercise of Congress's power to regulate interstate commerce, the Chief Justice went on to uphold the individual mandate under Congress's power to levy taxes.[128]

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[120] 15 U.S.C. §1011.

[121] 15 U.S.C. §1012 (b).

[122] 517 U.S. 25 (1996).

[123] P.L. 111-148, 124 Stat. 119.

[124] Codified at 26 U.S.C. §5000A.

[125] *NFIB v. Sebelius*, 132 S. Ct. 603 (2011).

[126] *NFIB*, 132 S. Ct. at 2586-87.

[127] Id.

[128] For a detailed analysis of the Court's decision in this case, see CRS Report R42698, *NFIB v. Sebelius: Constitutionality of the Individual Mandate*, by Erika K. Lunder and Jennifer A. Staman.

Appendix C. Past Insurance Regulatory Legislation and Proposals

Legislation in the 113th Congress

National Association of Registered Agents and Brokers Reform Act (S. 534, S. 1926, S. 2244, H.R. 1155/H.R. 1064, and H.R. 4871).[129]

The National Association of Registered Agents and Brokers Reform Act of 2013 (S. 534) was introduced in the Senate by Senator Jon Tester along with 13 cosponsors on March 12, 2013. The Senate Committee on Banking, Housing, and Urban Affairs' Subcommittee on Securities, Insurance, and Investment held a hearing on the bill on March 19, 2013.[130] The full committee amended the bill and ordered it reported on June 6, 2013.

Two identical bills, H.R. 1064 and H.R. 1155, were introduced in the House by Representative Randy Neugebauer. H.R. 1155 was introduced on March 14, 2013, with 42 cosponsors and additional cosponsors added since introduction, whereas H.R. 1064 has not had additional cosponsors added since its introduction with 41 cosponsors on March 12, 2013. H.R. 1155, with an amendment closely tracking the Senate committee amendment, was considered under suspension of rules and passed on a vote of 397-6 on September 10, 2013.

The National Association of Registered Agents and Brokers Reform Act would have established a National Association of Registered Agents and Brokers (NARAB). Apparently because the 1999 Gramm-Leach-Bliley Act[131] included provisions that could have created an identically named association, this legislation is often referred to as "NARAB II."[132] The NARAB II association would have been a private, nonprofit corporation. Its members, required to be licensed as an insurance producer in a single state and meet other requirements, would have been able to operate in any other state subject only to payment of the licensing fee in that state, rather than having to obtain a separate license in the additional states, as is often the case now. The association member would still have been subject to each state's consumer protection and market conduct regulation, but individual state laws that treated out-of-state insurance producers differently from in-state producers would have been preempted. The NARAB II association would have been overseen by a board made up of five appointees from the insurance industry and eight from the state insurance commissioners. The appointments would have been made by the President, and the President could have dissolved the board as a whole or suspend the implementation of any rule or action taken by the association. S. 534 and H.R. 1155 as amended were nearly identical in structure, except for slightly different language relating to background checks.

On January 29, 2014, the Senate added the text of S. 534 as amended to S. 1926, a bill addressing flood insurance, by voice vote. S. 1926 as amended passed the Senate the following day by a vote

[129] For more information, please see CRS Report R43095, *Insurance Agent Licensing: Overview and Background on Federal NARAB Legislation*, by Baird Webel.

[130] Hearing webcast and statements can be found at http://www.banking.senate.gov/public/index.cfm?FuseAction=Hearings.Hearing&Hearing_ID=72d49be4-ff44-4d01-862a-4654e13b2589.

[131] Specifically, P.L. 106-102, Title III, Subtitle C.

[132] GLBA included the provisional creation of a NARAB to streamline state insurance producer licensing for agents and brokers. The GLBA NARAB provisions, however, were not to go into effect if a majority of the states enacted uniformity in their insurance producer licensing laws and reciprocity for nonresident producer licensing laws. The states as a whole met these GLBA requirements, but some individual states never adopted reciprocity legislation.

of 67-32. The House, however, did not take up S. 1926, and P.L. 113-89 addressing flood insurance was ultimately enacted on March 21, 2014, without containing any NARAB provisions.

On June 19, 2014, the House Committee on Financial Services added the text of H.R. 1155 as amended to H.R. 4871, a bill addressing terrorism risk insurance, by voice vote. H.R. 4871 as amended was ordered favorably reported the following day by a vote of 32-27.

On July 17, 2014, the Senate adopted language nearly identical to H.R. 1155 as an amendment to S. 2244, a bill addressing terrorism risk insurance, by voice vote. The change introduced was a new Section 335 that would sunset the NARAB language two years after the association approves its first member. S. 2244 as amended passed the Senate on a vote of 93-4.

On December 10, 2014, the House passed a further amended version of S. 2244, including NARAB language but not including the Section 335 sunset provisions. The bill also included a new Title III related to derivatives legislation that had not been included in the Senate passed version. The House and Senate each adjourned on December 16, 2014, without resolving the differences between the versions of S. 2244 or passing other NARAB legislation.

Insurance Consumer Protection and Solvency Act of 2013 (H.R. 605)

H.R. 605 was introduced by Representative Bill Posey. This bill was referred to the House Committee on Financial Services and was one of the bills that was the subject of a hearing on May 20, 2014.

The Insurance Consumer Protection and Solvency Act of 2013 would have amended the Dodd-Frank Act so that insurance companies would have essentially no longer been subject to the resolution regime created in this law. It would have struck the Federal Deposit Insurance Corporation's (FDIC's) backup authority in the case of inaction by state authorities to resolve the insurance subsidiaries of financial holding companies and also excluded insurance companies from the FDIC's assessment authority to cover the cost of FDIC resolution.

Claims Licensing Advancement for Interstate Matters Act (H.R. 2156)

H.R. 2156 was introduced on May 23, 2013, by Representative Stephen Fincher along with two cosponsors. It was referred to the House Committee on Financial Services. H.R. 2156 would have encouraged uniformity and reciprocity among states that license independent insurance claim adjusters, but would not have applied to states that do not license adjusters. If, within four years of enactment, a state requiring licensure had not adopted laws providing for uniformity and reciprocity, as determined by the National Association of Insurance Commissioners (NAIC), H.R. 2156 would have provided that any licensed adjuster from another state could operate within such a state without licensure by that state. Such out of state adjusters would have still been liable to pay state fees as long as these fees were uniform regardless of the residency of the adjuster.

Insurance Capital and Accounting Standards Act of 2013 (H.R. 2140)

H.R. 2140 was introduced by Representative Gary Miller on May 23, 2013. It was referred to the House Committee on Financial Services.

H.R. 2140 would have created a presumption that insurance companies subject to Federal Reserve Board supervision[133] are in compliance with the minimum capital standards set by

[133] This would include insurers who are part of bank holding companies or savings and loan holding companies and insurers designated as systemically significant financial institutions (SSFIs) by the Financial Services Oversight

Section 171 of the Dodd-Frank Act[134] if they were in compliance with applicable state capital standards. The bill would have permitted the Federal Reserve, on a case-by-case basis, to overcome the presumption. To successfully overturn such a presumption, the bill would have required the Federal Reserve to have in place and to follow duly promulgated regulations defining the applicable procedures and standards to be followed in determining that an insurance company is not in compliance with state minimum capital standards and to have completed a cost-benefit analysis and a quantitative impact study. The bill also stipulated that governing state law continues to apply and specifies that the Federal Reserve would not have been able to require insurance companies that it regulates to comply with any accounting standards differing from those applicable under state law.

"A bill to clarify the application of certain leverage and risk-based requirements ... " (S. 2102)

S. 2102 was introduced by Senator Susan Collins on March 10, 2014. The Senate Committee on Banking, Housing, and Urban Affairs held a hearing on the bill the following day.[135] S. 2102 would have clarified Section 171 of the Dodd-Frank Act, popularly known as the Collins amendment. Section 171 put certain capital requirements on financial institutions under the oversight of the Federal Reserve. The Federal Reserve indicated that it viewed this section as requiring that the same standards be applied to both banks and insurers. S. 2102 would have amended Section 171 to specify that the federal banking agencies would not be required to include regulated insurance entities engaged in the business of insurance under the minimum capital requirements required by Section 171. S. 2102, however, would not have limited the authority of the Federal Reserve to apply capital standards.

Insurance Capital Standards Clarification Act of 2014 (P.L. 113-279/S. 2270 /H.R. 4510 /H.R. 5461)

S. 2270 was introduced by Senator Susan Collins along with four cosponsors on April 29, 2014. An amended version of the bill was agreed to on the Senate floor by unanimous consent on June 3, 2014. Upon receipt in the House, it was referred to the House Committee on Financial Services. The bill was discharged from the committee and passed on the House floor without objection on December 10, 2014. S. 2270 was signed into law (P.L. 113-279) by the President on December 18, 2014.

H.R. 4510 was introduced by Representative Gary Miller along with one cosponsor on April 29, 2014. It has been referred to the House Committee on Financial Services.

H.R. 5461 was introduced by Representative Andy Barr along with three cosponsors on September 15, 2014. Title I of the bill contains the Insurance Capital Standards Clarification Act as it was passed by the Senate, whereas Titles II, III, and IV contain other changes to the Dodd-Frank Act.[136] The House passed H.R. 5461 on September 16, 2014, under suspension of the rules on a vote of 327-97.

Council (FSOC).

[134] Codified at 12 U.S.C. §5371.

[135] U.S. Congress, Senate Committee on Banking, Housing, and Urban Affairs, *Finding the Right Capital Regulations for Insurers*, 113th Cong., 2nd sess., March 11, 2014.

[136] Title II addresses collateralized loan obligations; for more information see CRS In Focus IF10202, *Collateralized Loan Obligations (CLOs), Structure, Use, and Implementation of the Volcker Rule (In Focus)*, by Edward V. Murphy.

The Insurance Capital Standards Clarification Act is similar to S. 2102. It addresses the question of whether banks and insurers are required under Section 171 of Dodd-Frank to have the same capital standards applied by the Federal Reserve. As enacted, the act declares specifically that the same standards are not required under this section. In addition, the bill prevents the Federal Reserve from requiring that an insurer files financial statements according to Generally Accepted Accounting Principles (GAAP) if the company currently files statements with state regulators solely using Statutory Accounting Principles (SAP). It also includes the proviso that this provision would not limit the Federal Reserve from collecting information on an entity or group-wide basis.

Policyholder Protection Act of 2014 (H.R. 4557)

H.R. 4557 was introduced by Representative Bill Posey on May 1, 2014. The bill was the subject of a House Committee on Financial Services Subcommittee on Housing and Insurance hearing on May 20, 2014. H.R. 4557 would have amended the Federal Deposit Insurance Act[137] to declare that any regulation, order, or other action of the Board of Governors of the Federal Reserve System requiring a bank holding company to provide funds or other assets to a subsidiary depository institution shall not be effective nor enforceable with respect to an entity that is a savings and loan holding company that is also an insurance company, an affiliate of an insured depository institution that is an insurance company, or any other company that is an insurance company and that directly or indirectly controls an insured depository institution if (1) such funds or assets are to be provided by the entity and (2) the state insurance authority for the insurance company determines that such an action would have a materially adverse effect on the entity's financial condition.

Servicemembers Insurance Relief Act (H.R. 4669)

H.R. 4669 was introduced by Representative Edward Royce on May 19, 2014. The bill would have preempted state or local laws requiring members of the U.S. military, their spouses, or their dependents to change their auto insurance policies when they have temporarily moved to comply with any temporary duty or permanent change of station order. It was referred to the House Committee on Financial Services.

Captive Insurers Clarification Act (S. 2726/H.R. 5388)

S. 2726 and H.R. 5388 were introduced on July 31, 2014, by Senator Patrick Leahy and Representative Peter Welch, respectively. The bill was referred to the Senate Committee on Banking, Housing, and Urban Affairs and jointly to the House Committee on Financial Services and the House Committee on the Judiciary. S. 2726/H.R. 5388 would have amended the Dodd-Frank Act title on nonadmitted insurers to exclude captive insurers from the definition of a nonadmitted insurer.

Title III addresses the definition of points and fees in mortgage transactions, for more information see CRS Report R43081, *The Ability-to-Repay Rule: Possible Effects of the Qualified Mortgage Definition on Credit Availability and Other Selected Issues*, by Sean M. Hoskins. Title IV addresses margin requirements and derivatives; for more information see CRS Report R43117, *The Commodity Futures Trading Commission: Background and Current Issues*, by Rena S. Miller.

[137] 12 U.S.C. §18310-1.

Legislation in the 112th Congress

The National Association of Registered Agents and Brokers Reform Act of 2011 (H.R. 1112)

H.R. 1112 was introduced by Representative Randy Neugebauer along with 47 cosponsors on March 16, 2011. A similar bill was introduced in the 110th and 111th Congresses and passed the House in each Congress, but was not acted upon by the Senate. H.R. 1112 was referred to the House Committee on Financial Services.

H.R. 1112 would have established a National Association of Registered Agents and Brokers (NARAB). NARAB was to be a private, nonprofit corporation, whose members, required to be licensed as an insurance producer in a single state and meet other standards, would be able to operate in any other state subject only to payment of the licensing fee in that state. The NARAB member would still be subject to each state's consumer protection and market conduct regulation, but individual state laws that treated out-of-state insurance producers differently from in-state producers would be preempted. NARAB would be overseen by a board made up of five appointees from the insurance industry and four from the state insurance commissioners. The appointments would be made by the President, and the President could dissolve the board as a whole or suspend the effectiveness of any action taken by NARAB.

NARAB dates back to the Gramm-Leach-Bliley Act of 1999,[138] and the new legislation is often referred to as "NARAB II." GLBA included the provisional creation of a NARAB to streamline state insurance producer licensing for agents and brokers. The GLBA NARAB provisions, however, were not to go into effect if a majority of the states enacted uniformity in their insurance producer licensing laws and reciprocity for nonresident producer licensing laws. The states met these GLBA requirements. However, some states have not implemented uniformity and reciprocity laws.

The Risk Retention Modernization Act of 2011 (H.R. 2126)

H.R. 2126 was introduced by Representative John Campbell along with Representative Peter Welch on June 3, 2011. It was referred to the House Committee on Financial Services.

This bill would have expanded the Liability Risk Retention Act[139] (LRRA) federal preemption of state insurance laws, allowing risk retention groups (RRGs) to cover commercial property risks and risk purchasing groups (RPGs) to purchase coverage for commercial property risks. The bill would also have changed the enforcement mechanism for federal preemptions in the LRRA and added additional federal corporate governance, disclosure, and fiduciary duty requirements for RRGs under the act.

Under existing law, the federal preemptions in the LRRA are enforced through court action. If a risk retention group believes a state is attempting to regulate in a manner counter to the LRRA, it can bring suit in a federal court. H.R. 2126 would have created a process under which the director of the Federal Insurance Office could issue determinations as to whether a state's regulation of a RRG or RPG is preempted by the act. In addition, the director was to study and issue reports to Congress on the states' regulation of RRGs and RPGs and the compliance with the LRRA.

[138] Specifically, P.L. 106-102, Title III, Subtitle C.

[139] 15 U.S.C. §3901 *et seq*. For more information see CRS Report RL32176, *The Liability Risk Retention Act: Background, Issues, and Current Legislation*, by Baird Webel.

The corporate governance standards to be issued by the director of the FIO would have included requirements that (1) a majority of directors on an RRG's board be independent, (2) any audit committee be made up of independent directors, written governance standards be in place, and (3) contracts with service providers be limited to less than five years and be approved by the state insurance commissioner. Additional specific amendments to the LRRA would have expanded the consumer disclosure required in the act and imposed a fiduciary duty on the board of directors of a risk retention group.

The Insurance Data Protection Act (H.R. 3559)

H.R. 3559 was introduced by Representative Steve Stivers on December 5, 2011. It was marked up by the Subcommittee on Insurance, Housing and Community Opportunity of the House Committee on Financial Services on December 8, 2011, and approved for consideration by the full committee on a vote of seven to five. The bill was not brought before the full committee prior to close of the 112th Congress. H.R. 3559 was also referred to the House Committee on Agriculture, which did not act on the legislation.

This bill would have removed the Federal Insurance Office's authority to issue subpoenas in its information gathering efforts and exclude insurance companies from the Office of Financial Research's subpoena authority. It also would have extended existing FIO confidentiality requirements that apply to insurance information gathered by FIO to the sharing of such data by FIO or the gathering of such data by federal financial regulators.

The Insurance Consumer Protection and Solvency Act (H.R. 6423)

H.R. 6423 was introduced by Representative Bill Posey along with Representative Judy Biggert on September 14, 2012. It was referred to the House Committee on Financial Services. Although no hearings directly on H.R. 6423 were held, the bill in draft form was discussed in a subcommittee hearing in November 2011.[140]

H.R. 6423 would have amended Dodd-Frank so that insurance companies would essentially no longer be subject to the resolution regime created in this law. It would have struck the FDIC's backup authority to resolve insurance subsidiaries in the case of inaction by state authorities and excluded insurance companies from the FDIC's assessment authority to cover the cost of FDIC resolution.

Legislation in the 111th Congress

The Insurance Industry Competition Act of 2009 (H.R. 1583)

Representative Peter DeFazio and five cosponsors introduced H.R. 1583 in the House on March 18, 2009. H.R. 1583 was referred to the House Judiciary Committee, House Financial Services Committee and House Energy and Commerce Committee. No hearings or markups were held on the bill.

H.R. 1583 would have abolished the current exemption from federal antitrust laws for the "business of insurance" that dates to the McCarran-Ferguson Act of 1945 and removed a prohibition on investigations of insurance companies by the Federal Trade Commission. It would

[140] See U.S. Congress, House Committee on Financial Services, Subcommittee on Insurance, Housing and Community Opportunity, *Insurance Oversight and Legislative Proposals*, 112th Cong., 1st sess., November 16, 2011, http://financialservices.house.gov/calendar/eventsingle.aspx?EventID=268154.

not have changed the sections of the McCarran-Ferguson Act that give preeminence to state insurance regulators.

The National Insurance Consumer Protection Act (H.R. 1880)

Representatives Melissa Bean and Edward Royce introduced H.R. 1880 in the House on April 2, 2009. The bill was referred to the House Financial Services Committee, House Judiciary Committee, and House Energy and Commerce Committee. No further action was taken on the bill.

This bill would have created a federal charter for the insurance industry, including insurers, insurance agencies, and independent insurance producers. The federal insurance regulatory apparatus was to be an independent entity under the Department of the Treasury, and the federal law would have preempted most state insurance laws for nationally regulated entities. Thus, nationally licensed insurers, agencies, and producers would have been able to operate in the entire United States without fulfilling the requirements of each of the 50 states' individual insurance laws.

H.R. 1880 also addressed the issue of systemic risk by designating another entity to serve as a systemic risk regulator for insurance. The systemic risk regulator was to have the power to compel systemically significant insurers to be chartered by the federal insurance regulator. Thus, although the bill shared some similarities with past optional federal charter legislation, and would have allowed some insurers to choose whether to obtain a federal charter, it was not purely an optional federal charter bill.

The National Association of Registered Agents and Brokers Reform Act of 2009 (H.R. 2554)

This bill was introduced by Representative David Scott along with 34 cosponsors on May 21, 2009. A similar bill was introduced in the 110th Congress, where it passed the House but was not acted upon by the Senate. H.R. 2554 passed the House on March 3, 2011, and was subsequently referred to the Senate Committee on Banking, Housing, and Urban Affairs, but was not acted upon by the Senate.

H.R. 2554 would have established a NARAB. NARAB was to be a private, nonprofit corporation, whose members, once licensed as an insurance producer in a single state, would be able to operate in any other state subject only to payment of the licensing fee in that state. The NARAB member was still to be subject to each state's consumer protection and market conduct regulation, but individual state laws that treated out-of-state insurance producers differently than in-state producers would be preempted. NARAB would have been overseen by a board made up of five appointees from the insurance industry and four from the state insurance commissioners. The appointments were to be made by the President, and the President would have had the power to dissolve the board as a whole or suspend the effectiveness of any action taken by NARAB.

The Risk Retention Modernization Act of 2010 (H.R. 4802)

H.R. 4802 was introduced by Representative Dennis Moore (along with Representatives John Campbell and Suzanne Kosmas) on March 10, 2010. It was referred to the House Committee on Financial Services but was not acted upon further.

This bill would have expanded the federal preemption of state insurance laws, allowing risk retention groups to cover commercial property risks and risk purchasing groups to purchase coverage for commercial property risks. The bill would also have changed the enforcement

mechanism for federal preemptions in the LRRA, and added additional federal corporate governance, disclosure, and fiduciary duty requirements for risk retention groups under the act.

Under existing law, the federal preemptions in the LRRA are enforced through court action. If a risk retention group believes a state is attempting to regulate in a manner counter to the LRRA, it can bring suit in a federal court. H.R. 4802 would have created a process under which the Secretary of the Treasury could issue determinations as to whether a state's regulation of a RRG or RPG is preempted by the act. In addition, the Secretary of the Treasury and the Comptroller General would have studied and issued reports to Congress on the states' regulation of RRGs and RPGs and the compliance with the LRRA. The corporate governance standards to have been put into place by the bill would have included requirements that a majority of directors on an RRG's board be independent; any audit committee be made up of independent directors; written governance standards be in place; and contracts with service providers be limited to less than five years and be approved by the state insurance commissioner. Specific amendments to the LRRA would have expanded the consumer disclosure required in the act and imposed a specific fiduciary duty on the board of directors of a risk retention group.

The Federal License for Reinsurers Act of 2010 (H.R. 6529)

Representative Dennis Moore introduced H.R. 6529 on December 16, 2010. It was referred to the House Committee on Financial Services but no hearings or markups were held on the bill. H.R. 6529 would have created a federal license for reinsurers. The licensing and regulatory authority would rest with the FIO, which was created under the Dodd-Frank Act, which would have the authority to determine that state laws were inconsistent with federal law and thus preempted.

Administration Proposals

2008 Treasury Blueprint

In March 2008, then-Secretary of the Treasury Henry Paulson released a *Blueprint for a Modernized Financial Regulatory Structure*. Although the financial crisis had begun at that time, the Treasury blueprint was not primarily a response to the crisis, but instead an attempt to create "a more flexible, efficient and effective regulatory framework."[141] A wide-ranging document, the blueprint foresaw a completely revamped regulatory structure for financial services.

The 2008 Treasury model proposed a prudential regulator to oversee the solvency of individual companies, a business conduct regulator to oversee consumer protection, and a market stability regulator to oversee risks to the entire system. As an intermediate step, it made two specific recommendations on insurance regulation. First, it called for the creation of a federal insurance regulator to oversee an optional federal charter for insurers as well as federal licensing for agents and brokers. Second, recognizing that the debate over an optional federal charter was ongoing in Congress, it recommended the creation of an "Office of Insurance Oversight" in the Department of the Treasury as an interim step. This office would be charged with two primary functions: (1) dealing with international regulatory issues, including the power to preempt inconsistent state laws; and (2) collecting information on the insurance industry and advising the Secretary of the Treasury on insurance matters.

[141] U.S. Treasury, "Treasury Releases Blueprint for Stronger Regulatory Structure," press release, March 31, 2008, available at http://www.ustreas.gov/press/releases/hp896.htm.

President Obama's Financial Regulatory Reform Plan

In June 2009, the Department of the Treasury under Secretary Timothy Geithner released a white paper entitled *Financial Regulatory Reform: A New Foundation*, outlining President Obama's plan to reform financial regulation in the United States.[142] The plan did not foresee as complete an overhaul as did the 2008 blueprint, but it would have substantially changed the financial regulatory system. Specific changes called for included explicitly introducing systemic risk oversight by the Federal Reserve, combining the Office of Comptroller of the Currency and the Office of Thrift Supervision into a single banking regulator, and creating a new Consumer Financial Protection Agency.

Although the June report stated that the Administration was open to additional changes in the insurance regulatory system, the specific regulatory changes called for in the released legislative language were focused on areas other than insurance. Most insurance products, for example, were excluded from the jurisdiction of the new federal consumer protection agency. In general, the states were to continue to have a preeminent role in insurance regulation. Insurance regulation, however, would have been specifically affected through two other aspects of the President's plan: the regulation of large financial companies presenting systemic risk and the creation of a new Office of National Insurance within the Department of the Treasury.

Systemic risk regulation as proposed in the legislation would have been the primary responsibility of the Federal Reserve in conjunction with a new Financial Services Oversight Council made up of the heads of most of the federal financial regulators. The powers to regulate for systemic risk enumerated in the draft legislation extended to all companies in the United States engaged in financial activities. Although the draft legislation did not specifically name insurers as subject to federal systemic risk regulation, it would seem to have included them under federal jurisdiction. Companies judged to be a possible threat to global or U.S. financial stability could be designated Tier 1 Financial Holding Companies and made subject to stringent solvency standards and additional examinations. Such companies would also be subject to enhanced resolution authority rather than standard bankruptcy provisions. Although the draft language did make reference in some places to state functional regulatory agencies, it was left open exactly how the Federal Reserve as regulator of the financial holding company would interact with the state regulators of the individual insurance subsidiaries. Whether federal regulatory deferral to state regulators would have continued under the proposed legislation seemed an unresolved question.

Although systemic risk regulation would likely apply to a relatively small number of insurers, the called-for creation of an Office of National Insurance could have had a broader impact. Unlike the similarly named office in other legislation, such as H.R. 1880 in the 111th Congress, President Obama's Office of National Insurance would not have overseen a federal insurance charter or have had direct regulatory power over insurers. Rather, this office was to operate as a broad overseer and voice for insurance at the federal level, including collecting information on insurance issues, setting federal policy on insurance, representing the United States in international insurance matters, and preempting some state laws where these laws are inconsistent with international agreements.

[142] See http://www.treasury.gov/initiatives/Documents/FinalReport_web.pdf.

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