

STATEMENT  
OF  
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**PRESIDENT, OMNIA (Bermuda) LTD.**  
ON BEHALF OF THE  
**AMERICAN BANKERS INSURANCE ASSOCIATION**

TO THE  
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS  
OF THE  
UNITED STATES SENATE

***EXAMINATION AND OVERSIGHT OF THE CONDITION AND REGULATION OF THE  
INSURANCE INDUSTRY***

SEPTEMBER 22, 2004

Mr. Chairman and Members of the Committee, my name is Alan Liebowitz, and I am President of OMNIA (Bermuda) Ltd., an insurance company affiliated with the Old Mutual Financial Network. Old Mutual is a global diversified financial services network that extends from Europe to Asia, Africa and North America. In the United States, the Old Mutual Financial Network provides retirement savings and financial protection products in all 50 States through Fidelity & Guaranty Life, Americom Life & Annuity, and Fidelity & Guaranty Life of New York. Our life insurance companies have combined assets of over \$12 billion and serve nearly 650,000 policyholders. Prior to joining OMNIA, I was the general counsel for Citibank's insurance initiative and president of certain of its domestic insurance companies. During my 15 years at Citibank, I was actively involved in the efforts to permit Citibank's Delaware subsidiary bank to underwrite insurance.

I am here today on behalf of the American Bankers Insurance Association (ABIA). ABIA is a subsidiary of the American Bankers Association. ABIA's members are banking institutions that are engaged in the business of insurance and insurance companies and administrators that provide insurance products or services to banks.

Thank you for the opportunity to participate in this hearing on the condition and regulation of the insurance industry. We have concluded that the current insurance regulatory system is badly in need of reform and note that the organizations at this table agree with that fundamental premise. Virtually all industry participants and even insurance regulators have spent years detailing the failings of the State system and are now beginning to define appropriate solutions to the problem.

In general, the main criticisms of the State system include its lack of uniformity in licensing standards, its inability to bring insurance products to market within a reasonable time-frame, and the need for greater uniformity in oversight of market conduct.

In response to these criticisms, House Financial Services Committee Chairman Mike Oxley and Capital Markets Subcommittee Chairman Richard Baker developed a draft “Roadmap” for modernizing the State system of regulation. Recently, this “Roadmap” has been translated into an actual legislative proposal. The Oxley/Baker plan is comprehensive in scope and is the product of a long review process involving careful and thoughtful deliberation. We are pleased that the House has elected to begin legislating solutions to these problems and we look forward to working with the Chairmen as the legislative process moves forward.

Similarly, the States have made some progress with their plan for achieving uniformity. The National Association of Insurance Commissioners (NAIC) has focused its energies on the adoption of an Interstate Compact for life insurance products and the nationwide adoption of its Model Laws. ABIA is supportive of the NAIC’s work, as it represents a good faith effort towards achieving uniformity of regulation.

ABIA is not alone in trying to encourage the States and the Congress in their efforts to bring modernization to insurance regulation. Others share a similar goal and all of us want these efforts to succeed. However, while there are several approaches to modernizing insurance regulation, we have concluded that the best approach is the creation of a Federal chartering and regulatory system that serves as an alternative to the current State insurance regulatory system. Our approach requires the establishment of an “Optional Federal Charter”,

which addresses the shortcomings of the existing State insurance regulatory system, yet preserves the State system for those who prefer it.

In the balance of my Statement, I will explain the involvement of banks in the business of insurance; more fully describe the problems with the current system of State insurance regulation; explain our optional Federal chartering and regulation alternative; and, lastly, show how that alternative would protect and benefit consumers.

#### ABIA's Members Are Actively Engaged in the Business of Insurance

Banking institutions have long been involved in the business of insurance, principally as agents. The level and scope of that involvement has expanded significantly in recent years. ABIA estimates that in 2002, the banking industry produced almost \$70 billion in insurance premiums. This is a 26% increase over the 2001 estimate of \$55 billion in premiums. ABIA also estimates that there are over 2,000 banks involved in the distribution of insurance. This includes some of the nation's largest agent networks. In fact, we estimate that banking institutions employ over 50,000 licensed insurance agents.

Two laws passed by the Congress have contributed to the growth in bank insurance activities. First, the Riegle-Neal Interstate Banking and Branching Act of 1994 allowed banking organizations to establish nationwide offices through which they can offer insurance products and annuities. These multi-State offices not only have expanded bank insurance sales, but also have given our industry a unique exposure to the variations in State insurance laws and regulations. Second, the Gramm-Leach-Bliley Act authorized affiliations between banks and insurance companies. These affiliations have more closely aligned the banking

industry with the insurance industry, and have given ABIA an even deeper appreciation of the current State of insurance regulation.

### Problems With the Current Insurance Regulatory System

While the States have a commendable record of protecting consumers from insurance insolvencies, they also have a record of inconsistent and inefficient regulation that results in unnecessary costs and lost opportunities for consumers. In past testimony before the Congress, former NAIC president Ernst Csiszar described eight areas of insurance regulation in need of reform.<sup>1</sup> I will highlight the three areas of most importance to bank-insurance operations: producer licensing, rate regulation and product approval.

#### *Producer Licensing*

ABIA's members are particularly familiar with the patchwork of disparate laws applicable to the licensing of insurance agents. For example, different States impose different qualification and testing standards and different continuing education requirements. Licenses recognized in one State are not necessarily recognized in another State. Agents associated with banks are sometimes subject to sales limitations not applicable to agents not associated with banks. For organizations that operate agent networks in multiple States, these differences impose compliance costs and burdens that are both significant and ultimately borne by consumers.

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<sup>1</sup> Testimony of Ernst Csiszar, Director of Insurance, South Carolina Department of Insurance, before the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises of the Financial Services Committee, United States House of Representatives, Wednesday March 31, 2004.

Continued disharmony among States' producer licensing laws persists despite a considerable Congressional effort to eradicate it. In 1999, as part of the Gramm-Leach-Bliley (GLB) Act, Congress adopted two limited requirements designed to promote uniformity and reduce discrimination in the rules applicable to producer licensing and insurance sales. The first appears in Section 104 of the GLB Act. This Section includes a preemption standard designed to prevent the States from discriminating against depository institutions engaged in the sale of insurance. Following the enactment of Section 104, ABIA identified insurance sales laws in thirty-three States that by varying degrees conflict with and are preempted by the standard. We made this list available to State insurance authorities and the NAIC, urging them to repeal or otherwise not enforce the offending laws. Our appeal to the States continues to be largely ignored.

As a result, several National banks requested preemption opinions from the Office of the Comptroller of the Currency (OCC). Where OCC opinions have been issued (i.e., on State insurance sales laws in Massachusetts and West Virginia that are uniquely applicable to depository institutions), they have been the subjects of lawsuits in Federal courts. Those courts that have rendered judgment to date have ruled against the States. Even these judicial actions, however, have been ignored and have failed to cause other States to modify their laws.

The GLB Act also included provisions designed to encourage the States to reform their producer licensing laws and regulations. These so-called NARAB provisions required the establishment of an organization to develop uniform licensing rules and regulations but only if a majority of the States did not adopt either uniform or reciprocal licensing laws and regulations within three years of the date of enactment of the GLB Act. To facilitate

compliance with the GLB Act, the NAIC developed a reciprocal licensing Model Act, which has currently been adopted by only about 40 States. Because the States could avoid NARAB – and the uniformity mandate it represented - if only a majority of States enacted the Model, that action by a majority of States has allowed some States, including some of the largest States like California, to avoid the issue of licensing reform entirely.

And, the more important goal of achieving licensing uniformity has been put off indefinitely. The GLB Act allowed the goal of uniform agent licensing laws to remain unrealized so long as a majority of States passed reciprocal licensing laws. Unfortunately, reciprocity is not uniformity. Instead, it is the recognition and acceptance of differences between States. Five years after passage of the GLB Act, significant differences in State licensing laws remain.

### *Rate Regulation*

ABIA's members are also familiar with the anti-consumer effects of price controls. Congress repealed the last vestiges of Federal price controls on banking products over twenty years ago after it realized that such artificial constraints do more harm than good. Today, however, the insurance industry continues to be subject to extensive price regulation – to the disadvantage of consumers. In most States, an insurance product can only be sold after the State insurance regulator approves the price of an insurance product. Some States regulate the price of an insurance policy; some States regulate the loss ratio a given product line must maintain.

Price controls are only appropriate, arguably, when associated with a utility or a monopoly. In such situations, a single company could set and hold prices at unreasonable

levels. The insurance industry, however, is a competitive industry. There are thousands of insurers operating in the United States, and there are no significant barriers to entry for new companies. In such a competitive market, competition between firms will protect consumers from unfair pricing schemes much more efficiently than the government.

The consumer benefits associated with competitive rates are more than just speculative. Several States already have moved away from rate regulation, and, in those States, there is evidence that rates have fallen on certain products. A study by Scott Harrington for the AEI-Brookings Joint Center for Regulatory Studies entitled “Insurance Deregulation and the Public Interest” found that auto insurance is less costly and more available in 14 States that do not require prior approval of rates than in 27 other States that do require prior approval.

### *Product Approval*

Similar to price controls, most States’ insurance departments won’t approve an insurance policy for sale unless subject to prior review by the insurance regulator. ABIA’s members have found that the impediments created by most States’ prior approval requirements have had the undesirable effect of depriving consumers of innovative insurance products and retarded the ability of insurers to develop these products in a timely fashion.

Under the current State system of insurance regulation, it can take months, and sometimes years, for a company to receive permission from State insurance regulators to introduce a new product in every State. Such delays are an inevitable result of a system in which every State has an opportunity to review and approve insurance products and where the standards of review are different in every State. If the insurance industry cannot gain some

relief from the States' prior approval regime, life insurers will continue to lose market share to other non-insurance investment products and property and casualty insurers will reduce or eliminate their efforts to develop innovative products that offer more comprehensive benefits at lower costs.

### ABIA Supports Optional Federal Insurance Chartering

ABIA believes that the answer to the problems inherent in the current State insurance regulatory system is the creation of an optional Federal insurance chartering system for insurers and insurance agencies.

Seven years ago, ABIA developed its own "blueprint" for insurance regulatory reform patterned after the dual banking system. That blueprint called for the optional chartering of insurers and insurance agencies by either the Federal Government or the States. Our goal was not to replace or duplicate State insurance regulation, but to create an alternative to State insurance regulation. Optional chartering has worked well in the banking industry, and we saw no reason to believe it could not work well in the insurance industry.

When we first developed our blueprint, Congress was actively debating the Gramm-Leach-Bliley Act. Therefore, we put our blueprint on the back burner until action on that bill was complete. After the Gramm-Leach-Bliley Act was finalized, we made optional Federal chartering a priority. We converted our blueprint into a specific legislative proposal and unveiled it at a conference organized by the American Enterprise Institute in the fall of 2000.

Our optional Federal chartering proposal was a natural outgrowth of the banking industry's experience with the dual banking system. That system, which permits banking

institutions to voluntarily choose between a Federal or State charter, has been in place for over 140 years, and is widely perceived to be a great success.

Initially, our proposal received a mixed reception. State insurance regulators, some insurance trade groups, and representatives of consumer groups expressed various concerns and reservations. Other insurance trade groups offered quiet encouragement.

We soon joined forces with two other insurance trade groups, the American Council of Life Insurers and the American Insurance Association, each of which had developed its own proposal, to develop a common optional Federal chartering proposal. The first step in that cooperative effort was the development of a set of principles around which a legislative proposal could be structured. The second step was the drafting of a consensus bill. The end product incorporates the best of State insurance regulation into a single Federal/State optional chartering framework similar in structure to the dual banking system.

#### The Consensus Optional Federal Charter Proposal

The following are some of the key features of that consensus bill:

- *Office of National Insurance/National Insurance Commissioner* – The bill calls for the establishment of a new independent bureau within the Treasury Department, the Office of National Insurance. The National Insurance Commissioner, who would be empowered to charter, regulate and supervise National insurance companies and National insurance agencies, would head this office. The Commissioner would be a Presidential appointee, subject to Senate confirmation, and subject to a five-year term. The bill requires the establishment of a consumer protection division and a fraud

division within the Office. Start up funding for the Office would be provided by a loan from the Treasury, which must be repaid over 30 years. On-going funding would be provided by assessments imposed upon Federally chartered insurers and agencies.

- *National Insurers* – One of the central powers of the Commissioner would be the chartering of National insurance companies. Such companies could be organized in stock, mutual or fraternal form. As a general rule, National insurance companies would be subject to the exclusive regulation of the Office and the Commissioner. Federally chartered insurers would be required to obtain a license from the Commissioner to underwrite specific types (or lines) of insurance. A Federally chartered insurer could not be licensed to underwrite both life insurance and property and casualty insurance. However, the bill permits an insurance holding company to own both life and property and casualty insurers. The Commissioner would not issue a license for the underwriting of health insurance until three years after the date of enactment of the bill. Existing State licensed insurers could exchange a State license for a National charter and National license.
- *Solvency Regulations* – The Commissioner would be required to regulate the solvency of National insurers. For the first five years after the enactment of the bill, Federal solvency regulations would be based upon existing NAIC models, including the NAIC model accounting standards and the NAIC model risk-based capital standards.

- *Product Regulation* – As a general rule, a National insurer would not be subject to rate or form regulation. The Commissioner would be directed to develop policy standards for life insurance companies, and such companies would be required to file their forms with the Commissioner. However, these forms would not be subject to review or approval prior to their use by the company. Similarly, property and casualty companies would be required to file, annually, a list of standard policy forms, but, again, these forms would not be subject to prior review or approval. The Commissioner would review rates for long-term care insurance and disability insurance.
- *Market Conduct* – The Commissioner would be directed to issue regulations governing the market conduct of National insurers. Such regulations would address marketing and claims practices.
- *Corporate Organization* – The bill provides for insurance holding companies, which could own both State licensed and Federally chartered insurers. The bill also provides for changes in corporate control, demutualizations, mergers and acquisitions. These provisions are patterned after model State laws.
- *National Insurance Agencies* – The bill provides for the chartering of National insurance agencies and issuance of Federal producers' licenses. (Every National insurance agency would be required to hold a Federal producers' license.) Federally licensed producers could sell policies for any Federally chartered insurer or any State

insurer. States could not regulate sales of policies issued by Federally chartered insurers. However, States could require a Federal producer to obtain a limited license to sell policies issued by a State insurer. The limited license would subject the producer to State market conduct standards.

- *State Law* – As a general rule, National insurers, National insurance agencies and Federally licensed producers are not subject to State insurance regulations. However, Federally chartered property and casualty companies would be subject to State reparations statutes, which define the scope of property and casualty policies. Also, National insurance agencies that sell policies for State licensed insurers may be required to obtain limited State licenses. National insurers also would be subject to State tax laws, including premium tax requirements.
- *Insolvencies* – The bill includes receivership provisions patterned after a model Interstate Insurance Receivership Compact proposal developed in 1998. Under those provisions, Federal courts, not State courts, would handle the receiverships of National insurers. The bill requires National insurers to be members of the State guarantee associations in those States where they do business. However, if a State’s guaranty statute does not provide policyholders certain minimum standards of protection, a Federal guarantee association would step in and guaranty the policies issued by insurers operating in that State. States are given four years to meet these minimum standards.

In sum, the bill provides insurers and agencies a chartering and supervisory alternative to State insurance regulation. It does so in a manner that safeguards the interests of policyholders and the public-at-large. It also does so in a manner that preserves the integrity of State regulations. State authority over State-licensed insurers and agencies is untouched. State authority to tax all insurers and agencies is recognized. State guaranty systems are left in place.

### Consumer Protections and Optional Federal Chartering

ABIA's member companies are driven by the needs and demands of consumers, so we recognized early on that any insurance modernization proposal must be responsive to those needs and demands. ABIA believes the consensus optional Federal charter proposal benefits consumers in several respects: It assures consumers access to sound insurance products in a fair manner; It is responsive to the changing needs of consumers; and, It creates a dynamic tension between State and Federal regulators that is in the best interests of consumers.

#### *Federal Solvency and Market Conduct Standards Ensure That Consumers Have Access to Sound Insurance Products in a Fair Manner*

Optional Federal regulation of insurers and producers fully and fairly protects the rights and interests of the consumers of insurance through Federal solvency standards. These standards include risk-based capital requirements (which will ensure that National insurers are adequately capitalized); Investment standards (which require a National insurer to invest assets prudently); and, Dividend restrictions (which prevent insolvent National insurers from

paying dividends). Such standards give consumers confidence that a Federally chartered insurer is able to pay claims on its policies.

The consensus proposal backs Federal solvency standards with regular examinations and enforcement actions. These examination and supervisory powers signal to consumers that Federally chartered insurers are safe and sound. Examination and enforcement standards include the authority to require Federally chartered insurers to file regular reports on their operations and financial condition; the authority to regularly examine Federally chartered insurers, and to the extent appropriate, their affiliates; and the authority to initiate an enforcement action against Federally chartered insurers that fail to comply with applicable standards. Enforcement penalties are patterned after those available to Federal banking regulators, which include the power to remove officers and directors and to impose civil money penalties of up to \$1 million a day.

Optional Federal chartering also protects consumers through Federal market conduct standards. Such standards protect consumers by preventing unfair methods of competition and unfair and deceptive acts and practices in the advertising, sale, issuance, distribution and administration of insurance policies.

Critics of optional Federal chartering often claim that a Federal insurance regulator would not be able to adequately police sales and claims practices by National insurers or producers. Some of these critics even cite the hundreds of thousands of consumer complaints filed annually with State insurance regulators in support of this claim. The Federal regulation of the banking industry shows that Federal agencies can effectively enforce consumer protection standards.

Today, thousands of banks are offering a variety of products to consumers through hundreds of thousands of branches, ATMs, loan production offices and other outlets throughout the United States. These banks are subject to Federal consumer protection statutes such as the Truth-in-Lending Act, the Truth-in-Savings Act, the Fair Credit Reporting Act, the Equal Credit Opportunity Act and many others. The Federal banking agencies, which are responsible for enforcing compliance with these various consumer protection laws, have been able to fully and effectively enforce compliance with the laws. They have done so through a combination of regular examinations and the threat of enforcement actions. Federal market conduct standards for insurers backed by examinations and the threat of enforcement should work equally well for the consumers of insurance.

In fact, the combination of Federal market conduct standards backed by regular examinations and the potential for enforcement actions should provide insurance consumers better protection than currently exists in many States. The number of consumer complaints filed annually with State insurance commissioners is not a sign of successful State market conduct regulation. Those complaints indicate that something is wrong with State market conduct regulation — otherwise consumers would not need to file so many complaints. The fact is that many States do not conduct market conduct examinations, and this allows insurers and producers who choose to ignore the laws to engage in practices that are harmful to consumers. Federal market conduct standards, regular examinations and the threat of enforcement actions would effectively deter such harmful practices.

### *Access to Uniform Products Benefits Consumers*

Uniform policies and sales practices reduce consumer confusion, especially for those consumers that move from State to State for professional or personal reasons. Under an optional Federal chartering system, the same life insurance policy could be offered in every State. Optional Federal chartering also would permit a company to use the same policy form, same disclosure Statements, and same administrative procedures throughout the United States.

Uniform regulation also facilitates delivery of insurance products over the Internet. As we all know, the Internet can reach consumers, regardless of where they are located. To date, however, the use of the Internet to deliver insurance products has been complicated by variations in State insurance sales laws. A single Federal sales practice standard would not be subject to such complications. This would expand consumer access to insurance products through the Internet.

### *The Dynamic Tension Created by Optional Federal Chartering Benefits Consumers*

The model for optional Federal chartering is the dual banking system. Since the dual banking system has been in place for over 140 years, the best way to judge how optional Federal chartering for insurers and producers would affect consumers of insurance is to take a closer look at the dual banking system.

It is interesting to note that the authors of the dual banking system were President Lincoln and his Secretary of the Treasury, Salmon Chase. After he became President, Lincoln worked with Secretary Chase to secure enactment of the National Bank Act, which provided for the chartering and regulation of National banks.

While there is evidence that President Lincoln intended National banks to replace the then existing system of State banks; that has not been the case. Today, approximately two-thirds of all banks are State chartered, and those banks control approximately 40 percent of all banking assets. We are confident the same dynamics prevalent in the banking industry will emerge in the insurance industry. Accordingly, contrary to the concerns of State insurance regulators, in our opinion, optional Federal regulation will not replace State regulation.

In sum, we see no reason to believe that the dynamic tension inherent in a dual regulatory system would not produce a strong supervisory environment for insurance firms and lead to the development of new products and services for insurance customers, just as it has done for the banking industry and banking customers.

### Conclusion

In conclusion, we urge the Committee to carefully consider the weaknesses of the current State system of insurance regulation and the merits of ABIA's optional Federal insurance chartering proposal. I again thank you for the opportunity to appear here today and if we can be of any further assistance as you consider this issue, I hope the Committee will call upon us.