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on

Streamlining Regulation, Improving Consumer Protection and Increasing Competition in Insurance Markets

Mr. Chairman, Ranking Member Johanns, Members of the Subcommittee,

Thank you for the opportunity to testify before the subcommittee. My name is Baird Webel. I am a Specialist in Financial Economics at the Congressional Research Service. This statement responds to your request for testimony addressing the general topic of today's hearing and particularly legislation before the subcommittee. My written testimony begins with a discussion of some general approaches that Congress has taken in addressing insurance regulation in the past and this is followed with a section addressing insurance producer licensing, past proposals for a National Association of Registered Agents and Brokers, and S. 534, the National Association of Registered Agents and Brokers Reform Act of 2013. The testimony concludes with an appendix providing general background on insurance regulation drawn from forthcoming and past CRS reports.

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Insurance Regulation and Federal Legislation

The individual states have been the primary regulators of insurance in this country for the past 150 years. The 1945 McCarran-Ferguson Act specifically authorized the states' role and Congress has recognized state primacy in insurance regulation in more recent laws shaping the financial regulatory system, such as the Gramm-Leach-Bliley Act (GLBA), also known as the Financial Services Modernization Act of 1999 (P. L. 106–102), and the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act; P.L. 111-203). Although Congress may have generally reaffirmed the state-based system in such laws, the operation of the system has continued to be of interest to Congress, as evidenced, for example, by this hearing today.

Legislative proposals to change various aspects of the insurance regulatory system have been introduced periodically over the years since 1945. These proposals have ranged from relatively minor adjustments to completely rethinking the role of the federal government in the system. The approaches considered by Congress in the past have included:

Creation of a Broad and Optional Federal Regulatory System for Insurance

Examples of this include several different bills calling for an optional federal charter for insurers akin to the current dual banking regulatory system, in which a bank may receive a charter from either an individual state or a federal regulator. The most recent such legislation to be introduced was H.R. 1880 in the 111th Congress, which was referred to the House Committee on Financial Services.

Creation of a Federal Regulatory System for Particular Types of Insurance

In the discussion over the past decade about the possibility of increased federal involvement in insurance issues, arguments are sometimes made regarding the differing local characteristics of insurance, which is particularly applicable to property/casualty insurance. Some have thus suggested that, rather than a full-scale federal charter for insurance, it would be more appropriate to have federal regulation for lines of insurance that face largely the same characteristics across the country. During House committee consideration of legislation (H.R. 2609, 111th Congress) incorporated into the Dodd-Frank Act, amendments were offered to create a federal charter for reinsurers and to create a federal charter for bond insurers. These amendments were withdrawn before being voted upon in committee. The reinsurer amendment was also offered as a stand-alone bill (H.R. 6529, 111th Congress), which was referred to the House Committee on Financial Services.

Expansion of Other Federal Regulatory Powers to Include Insurance

Federal oversight on insurance could be implemented from entities that are not set up specifically to address insurance. For example, legislation (H.R. 3126, 111th Congress) incorporated into the Dodd-Frank Act initially would have authorized the Consumer Financial Protection Bureau to oversee title, credit, and mortgage insurance, although the final bill did not do so. The Federal Reserve, following the Dodd-Frank Act, regulates holding companies that have banking subsidiaries, including many whose primary business is insurance, as well any companies designated by the Financial Stability Oversight Council (FSOC) as systemically important, which could include insurance companies.

Federal Preemption of Multiple State Regulatory Authority in Favor of a Single State

Congress took this approach in the Liability Risk Retention Act (LRRA; 15 U.S.C. §3901 *et seq*), which was enacted in 1981 and amended in 1986. The LRRA allows a limited range of state-chartered insurance companies to operate throughout the country without licenses from the individual states. Other examples include the Nonadmitted and Reinsurance Reform Act (NRRA), which was enacted as part of the Dodd-Frank Act. The NRRA provides that the home state of the insurance consumer would have primary tax and regulatory authority over surplus lines insurance.

Broad Federal Standard Setting to be Carried Out by Other Entities

The National Association of Registered Agents and Brokers (NARAB) provisions of the Gramm-Leach-Bliley Act, which would be further amended by S. 534 under discussion today, are a primary example of this sort of approach. Congress sets the broad goals of uniformity and reciprocity in insurance producer licensing but creates a private body with the authority to fill in the details and manage the process. Another example would be a provision of the NRRA, which preempts state laws on eligibility of surplus lines insurers if they conflict with National Association of Insurance Commissioner (NAIC) model laws.

Insurance Producer Licensing and NARAB

Licensing of insurance agents and brokers (known generally as "producers") has long been an integral part of the insurance regulatory system. Individual states typically require that insurance producers operating within their borders obtain a license from that state, and different licenses are also often required for different lines of insurance. Such licensure provides a mechanism for insurance regulators to enforce standards of conduct, particularly with regard to consumer protections, as well as providing a revenue source to help defray the cost of the insurance regulatory system. Aspects of insurance producer licensing include specific education or knowledge requirements, such as continuing education, and, in some states, criminal background checks. The NAIC has adopted model laws regarding licensure and a model insurance producer license form, but individual states are free to modify NAIC models, or not adopt them at all, resulting in variability in licensing requirements across the country. Insurance producers who operate in multiple states have long sought increased uniformity and reciprocity across states to reduce their costs resulting from the multiplicity of license requirements.

In addition to the costs that might result from the specific aspects of the insurance licensing system, any professional licensing regime acts as a barrier to entry for those who might be interested in providing services that require a license. Economic theory suggests that such barriers increase consumer costs to some degree and have the potential to be used as a protectionist measure to prevent competition, allowing license-holders to extract economic rents from consumers. Whether or not the public benefits resulting from licensure outweigh the costs is a decision to be evaluated on a case-by-case basis by public policymakers. Some form of licensure for those in the financial services industry has been generally accepted and is required in federal law for people involved in securities transactions with the public, for example.

GLBA and NARAB I

Provisions in the Gramm-Leach-Bliley Act sought to address insurance producer complaints about the variation in state licensing requirements through a sort of provisional federal preemption of state laws. The law called for the creation of a private, non-profit licensing body, the National Association of Registered Agents and Brokers, whose insurance producer members would have been authorized to operate across state lines without individual licenses from every state. While backed by federal authority, the NARAB to be created by the provisions in GLBA (hereafter referred to as "NARAB I") would have been entwined in the system of state regulation. Membership in NARAB I would have been open only to people already holding a state insurance producer license and the NAIC would have appointed the members of the NARAB I board and had other oversight authorities.

The NARAB I language in GLBA also offered the states the opportunity to avoid creation of the NARAB I organization if a majority of the states created among themselves systems of either uniformity or reciprocity in insurance producer licensing within a three-year window after passage of GLBA. The NAIC was given the authority to determine whether the states met the GLBA standard with the possibility of federal judicial review of this determination. The individual states and the NAIC reacted relatively quickly to this opportunity with the promulgation of an NAIC model law that would provide for reciprocity and the adoption of laws providing for reciprocity in sufficient number of states that the NAIC determined the GLBA standards were met; as a result, the NARAB I organization was not created.

The GLBA statutory requirements for reciprocity may have been satisfied by 2002, but insurance producers continued to identify inefficiencies and costs of the state licensing system in the years following. In 2008, testimony before a House subcommittee, for example, an insurance agent representative indicated that states continued to "impose additional conditions and requirements"[1] on non-resident agents despite the reciprocity called for in law. In 2009, the Government Accountability Office (GAO) cited issues regarding fingerprinting and background checks as particular barriers to uniformity or reciprocity in producer licensing and as potentially posing a problem for insurance consumer protection. GAO also found differences in licensing requirements and insurance line definitions as potentially creating inefficiencies that "could result in higher costs for insurers, which in turn could be passed on to consumer[s]."[2] In addition to concerns about the substance of the reciprocity in place, reciprocity laws have not been adopted by every state. The NAIC certified 47 states as reciprocal, but the three states not certified were California, Florida, and Washington, which together have nearly 20% of the nation's population.

Concerns about the effect, or lack of effect, of the NARAB I provisions have prompted some Members of Congress to seek a further legislative solution.

NARAB II Legislation

Legislation to mandate the creation of a NARAB organization (hereafter referred to as NARAB II) was first introduced into the House of Representatives in the 110th Congress (H.R. 5611), with similar legislation in the 111th Congress (H.R. 2554). The House passed these bills in both Congresses by voice vote, but the legislation was referred to committee when received by the Senate. NARAB II legislation was introduced in the 112th Congress (H.R. 1112) and the 113th Congress (H.R. 1155). Unlike the previous Congresses, the House did not bring H.R. 1112 to the floor in the 112th Congress. H.R. 1155 has been referred to committee in this Congress. Senate legislation to create NARAB II was first introduced in the 112th Congress (S. 2342), with the bill reintroduced in this Congress as S. 534.

Although specific legislative provisions, such as the precise makeup of the NARAB organization's board, have changed in the various iterations of NARAB II legislation, the bills have retained the same essential purpose. The bills would amend the NARAB sections from GLBA to remove the conditionality and instead create a NARAB organization regardless of state actions on reciprocity and uniformity. The NARAB II legislation would create an organization very similar to that originally envisioned in GLBA. It would be a non-profit, private body,

[1] Statement Of Tom Minkler on behalf of the Independent Insurance Agents & Brokers Of America, Subcommittee on Capital Markets, Government Sponsored Enterprises, and Insurance, Committee on Financial Services, United States House of Representatives, April 16, 2008, p. 6, available at http://archives.financialservices.house.gov/hearing110/minkler041608.pdf.

[2] U.S. Government Accountability Office, *Insurance Reciprocity and Uniformity*, GAO-09-372, April 6, 2009, p. 21, http://www.gao.gov/products/GAO-09-372.

whose members would be required to be state-licensed insurance producers, but who would also be able to operate across states without having licenses from the individual states.

Among the differences between the NARAB II proposed in S.534 and the original NARAB I are

- *Appointment of the Board*:
  NARAB I was to have a seven-member board appointed by the NAIC.[3] S. 534 specifies a 13-member board appointed by the President and confirmed by the Senate. Eight of the 13 are to be state insurance commissioners, with the remainder being representative of the insurance industry.
- *Oversight by the NAIC*:
  In addition to the board appointments, NARAB I provided several other methods of NAIC oversight, including NAIC approval of NARAB bylaw changes and rules, and NAIC review of disciplinary actions.[4] S. 354 gives much less direct authority to the NAIC. For example, NARAB II would file changes to bylaws with the NAIC, but the NAIC would not have the authority to disapprove the changes.
- *Criminal Background Checks*:
  S. 354 requires a federal criminal background check prior to membership in NARAB II and provides for the performance of these checks by the U.S. Attorney General, including the authority of the Attorney General to charge fees to defray the costs incurred. There were no similar provisions on background checks in GLBA for NARAB I.

[3] The NAIC could lose this appointment authority if (1) states representing 50% of the total commercial lines insurance premiums did not satisfy uniformity or reciprocity requirements and (2) the NAIC had not approved the bylaws or was unable to supervise the organization.

[4] The NAIC could lose its oversight authority under the same conditions as the possible loss of its board appointment authority.

Appendix. Background on Insurance and Insurance Regulation

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/health companies in 2011 totaled $581.4 billion and premiums for property/casualty insurance companies totaled $436.0 billion.[5] Assets held by the insurance industry totaled approximately $7.5 trillion according to the National Association of Insurance Commissioners (NAIC).

Different lines of insurance present very different characteristics and risks. Life insurance typically is a longer-term proposition with contracts stretching into 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 healthcare delivery, including negotiating contracts with physicians and hospitals and a regulatory system much more influenced by the federal government through Medicare, Medicaid, the Employee Retirement Income Security Act of 1974 (ERISA),[6] and the Patient Protection and Affordable Care Act (ACA).[7] This testimony will concentrate primarily on non-health insurance.

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.[8] 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.[9] 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.[10] The

[5] Premium amounts used are net premiums written from AM Best, *2012 Statistical Study: U.S. Property/Casualty - 2011 Financial Results*, March 26, 2012, and AM Best, *2012 Statistical Study: U.S. Life/Health - 2011 Financial Results*, March 28, 2012.

[6] P.L. 93-406, 88 Stat. 829.

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

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

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

[10] 15 U.S.C. §1011 *et seq.*

act's primary purpose was to preserve the states' authority to regulate and tax insurance.[11] The act also granted a federal antitrust exemption to the insurance industry for "the business of insurance."[12]

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 (LRRA) created by Congress in 1981 and amended in 1986.[13] In general, however, when proposals were made in the past[14] 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 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 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.[15]

[11] 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).

[12] 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.

[13] 15 U.S.C. §3901 *et seq.* See CRS Report RL32176, *The Liability Risk Retention Act: Background, Issues, and Current Legislation*, by Baird Webel.

[14] 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.

[15] See, for example, "17-Year Sentence Affirmed for Investor Who Looted Insurers," *New York Times*, March 24, 2006, available (continued...)

Another state reform largely implemented in the late 1980s and early 1990s was the introduction of state insurance guaranty funds.[16] 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[17] and $300,000 for life insurance death benefits and $100,000 for life insurance cash value and annuities.[18] 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)[19] 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 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.[20]

(...continued)

at http://www.nytimes.com/2006/03/24frankel..html?ref=martinfrankel.

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

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

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

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

[20] 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 more on the charter of the institution so, for example, banking regulators oversee all the activities of a bank even if the bank is offering insurance products.

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.[21]

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.

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 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.[22]

[21] 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.

[22] See CRS Report RS21827, *Insurance Regulation After the Gramm-Leach-Bliley Act*, by Carolyn Cobb.

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.[23] 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[24] 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 see 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 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.

[23] 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. Treasury and available at http://www.treasury.gov/press-center/press-releases/Documents/Blueprint.pdf.

[24] 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.

The second failure in the insurance industry was that of a specific company, American International Group.[25] 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 have followed, including nearly $70 billion through the U.S. 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 sale by the U.S. Treasury 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,[26] which enacted broad financial regulatory reform. Although the Dodd-Frank Act had a number of provisions that directly and indirectly addressed insurance, it left the states as the primary functional regulators of insurance. The Dodd-Frank Act provisions that most directly addressed insurance and are of ongoing concern were (1) creation of a Federal Insurance Office (FIO); (2) systemic-risk provisions, such as the creation of a Financial Stability Oversight Council (FSOC) with the authority to oversee systemically important insurers; and (3) previously introduced provisions harmonizing the tax and regulatory treatment of surplus lines insurance and reinsurance (the Nonadmitted and Reinsurance Reform Act).[27] Provisions in the law regarding holding company oversight could also affect a number of companies who are primarily insurers, but who also have banking or thrift subsidiaries and are thus overseen by the Federal Reserve following the Dodd-Frank Act.

Attention on insurance regulation in the 112th Congress 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 FSOC designating some insurers and systemically important and thus subject to additional oversight. Neither issue reached a resolution during the 112th Congress.

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[25] See CRS Report R40438, *Federal Government Assistance for American International Group (AIG)*, by Baird Webel.

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

[27] 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.