Statement of

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on behalf of

NAIFA

NATIONAL ASSOCIATION OF
INSURANCE AND FINANCIAL ADVISORS

Before

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Regarding

Regulatory Restructuring: Enhancing Consumer
Financial Products Regulation

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Good morning Chairman Frank, Ranking Member Bachus and Committee members. My name is Cliff Wilson and I am the president of the National Association of Insurance and Financial Advisors (NAIFA). Thank you for the opportunity to appear before you today to share our views regarding financial regulatory reform and the critically important area of consumer protection.

NAIFA comprises more than 700 state and local associations representing the interests of approximately 200,000 agents and their associates nationwide. NAIFA members focus their practices on one or more of the following: life insurance and annuities, health insurance and employee benefits, multiline, and financial advising and investments. The Association's mission is to advocate for a positive legislative and regulatory environment, enhance business and professional skills, and promote the ethical conduct of its members. NAIFA's website can be accessed at www.naifa.org.

I read with interest President Obama's regulatory reform proposal, "A New Foundation: Rebuilding Financial Supervision and Regulation," and listened intently to Treasury Secretary Geithner's testimony before the Senate Banking Committee last week. NAIFA members share the views of the Administration and this Committee that protecting consumers is the ultimate purpose of regulation and that robust consumer protection is necessary to ensure public trust in financial products and services and in the financial system as a whole. We see the impact of strong consumer protection laws and rules every day and, despite the burden in cost and time to us as producers, believe in the benefits they bring to our customers.

Moreover, we understand the desire for improved regulatory oversight of products and services that have, to date, been un-regulated or under-regulated. The fact is that many financial products are not subject to the same level of oversight as insurance products and, because of current regulatory structures, may fall into regulatory "gaps," thus escaping meaningful supervision and / or enforcement of current protections. Stepped-up federal oversight through a Consumer Financial Protection Agency (CFPA) may make sense for these products.

Insurance, however, is different for the following reasons, which I will address more fully below:

> (1) Insurance products currently are subject to comprehensive state insurance regulatory oversight, which places a strong emphasis on consumer protection;
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> (2) It is dangerous to separate insurance product regulation from solvency regulation because the pricing and cost of products is so interrelated to the financial health of the insurer offering the product; and
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> (3) There is no insurance expertise or regulatory infrastructure within the federal government to support a CFPA. To the extent the federal government assumes insurance product regulatory authority, it should be part of a comprehensive insurance regulatory reform effort that brings the required insurance expertise to Washington, addresses regulatory overlap with the states, and has the authority to address the full panoply of regulatory issues that arise in connection with the oversight of this critical sector of the economy.

For these reasons, unless and until comprehensive insurance regulatory reform results in federal regulation of insurance, insurance products should not be placed under the authority of a federal financial products agency. Such oversight is not workable, nor is it necessary, in the insurance context.

Let me address each of these differences more fully.

(1) Insurance products are subject to comprehensive state regulatory oversight; federal intervention is unnecessary and could lead to regulatory confusion.

The states have been the primary regulators of insurance for 150 years. State insurance regulatory authority was affirmed by Congress in 1945, with enactment of the McCarran-Ferguson Act, and, more recently, with the Gramm-Leach-Bliley Act and its functional regulation structure. Today, each state, plus the District of Columbia and the five United States territories, has in place a comprehensive cradle-to-grave insurance regulatory regime that covers the universe of issues from corporate structure, to solvency, to consumer protections (market conduct), to product regulation.

Insurers, insurance agencies, and insurance agents are required to comply with the laws and rules of every state in which we do business and are required to hold a license in every such state. Agents that sell more than one line of coverage may be required to hold more than one license in each state. As part of the licensure process, most states require agents to undergo pre-licensing and continuing education courses, pass examinations, submit to an application process, and, perhaps most important, comply with state consumer protection laws.

Moreover, agents cannot sell a product in a state unless it has been approved by the state's insurance regulator. Product approval is an extensive process by which regulators review products for sale in their states. Until fairly recently, it was a state-by-state endeavor that could take years to complete. With the adoption in 2003 of the NAIC's Interstate Insurance Product Regulation Compact, the product approval process for life insurance, annuities, long-term care, and disability income products has been streamlined dramatically, even as the regulatory review and analysis of products has been maintained. The Compact became operational in 2006, when it was adopted by 26 states (states with over 40 percent of the premium volume for the covered products). Since that time, the Interstate Insurance Product Regulation Commission (IIPRC) has approved approximately 175 products for sale in the now 35 compacting states and territories (which represents over 50% of the premium volume in for the covered products).

In addition to product approval, many states require approval of the rates charged for many insurance products, particularly property and casualty products and health insurance. Most, if not all, states require that rates not be excessive, inadequate, or unfairly discriminatory. Some states require that a rate be approved prior to use, some allow a rate to be used unless the regulator subsequently disapproves it for failing to meet regulatory requirements. Still other states impose "flex-rating" laws that do not require prior approval for rate changes unless they exceed certain parameters.

More than 40 states have also imposed suitability requirements in connection with the sale of annuity products. The NAIC's "Suitability in Annuity Transactions Model Regulation" (Model) imposes a suitability requirement on any recommendation to purchase or exchange an annuity – be it fixed or variable. With respect to the purchase and exchange of variable annuities, the rule imposes a duty on insurance companies where none previously existed. In addition to this requirement, more than 80% of NAIFA members are securities licensed and subject to FINRA rule 2821 with regard to the sale of variable products. The NAIC Model expressly states that compliance with FINRA suitability rules satisfies suitability requirements in the Model with respect to the sale of variable annuities. It is important to keep in mind that for agents/registered representatives selling variable annuities in states that have not enacted the Model, the FINRA requirements still apply.

I could go on at length describing the states' consumer protection and product oversight rules and requirements, but suffice it to say that the states have a thorough process that provides robust consumer protections. The specifics of the President's financial regulatory reform proposal have yet to be fleshed out, so it is impossible to know with certainty what the role of the CFPA will be with respect to insurance products. We have a pretty good sense, however, that it was designed to be able to cover at least some insurance products – those deemed to be "payment products and other consumer financial products and services" – and the providers of such products and services. Annuities could be slotted into these categories. We also know that the CFPA would have authority to implement and enforce regulations, including a wide array of new disclosure obligations.

What is unclear – and what may, in practice, remain unclear if the legislation is enacted to encompass insurance products – is where federal authority would stop and current state regulatory authority would remain. The danger is that we could end up with a dual regulatory structure in which the authority of the states is undercut, or at least put into question. This uncertainty with respect to the finality of regulatory decisions will hinder the industry's ability to effectively serve consumers and could lead to a chilling effect in connection with the development of new life insurance, annuity or other traditional insurance products like long-term care and disability income products in new markets – just at a time when we should be encouraging people to plan for their futures.

Moreover, to the extent that one of the missions of the CFPA would be to simplify consumer disclosures, we are unsure how that can be accomplished under a regime that would establish a regulatory floor under which state disclosure requirements would still be fully applicable. It appears that these twin objectives – disclosure simplification and the continued applicability of current state requirements – are at odds with one another and that all the new federal requirements would accomplish in the highly regulated insurance arena would be to add an additional set of duplicative requirements.

(2) Separation of insurance product regulation from insurance solvency regulation is dangerous.

In an apparent effort to avoid undercutting solvency regulation and thereby causing market disruptions, the CFPA would be required to consult with other federal regulators to promote consistency with solvency, market and systemic objectives, and to share regulatory information with those regulators. Having said that, there is no similar requirement to work with state insurance regulators, and this is cause for serious concern.

We believe it is extremely dangerous to separate product regulation from solvency regulation. The states regulate solvency to ensure that the ultimate consumer protection is available when needed – the promise to pay when a claim comes due. A regulator focused only on one part of the puzzle – product oversight – may take actions with the best of intentions to regulate a product, but without sufficient knowledge or understanding of the industry or marketplace, those actions could have the effect of undercutting the solvency of the insurer providing that product. So in the long term, the consumer is not protected at all.

We have some first-hand experience with this that few of you are likely to recall. In 1979-1980, the Federal Trade Commission (FTC) attempted to impose regulations with respect to life insurance products. The FTC made assumptions about the returns on these insurance products vis-á-vis mutual funds and other investment products that were misleading for the consumers of those products. Because of the FTC's lack of understanding of the products and of the insurance industry more generally, the assumptions it made were incorrect, or at least misleading, and it took an act of Congress to fix the situation.

This is why we are very sensitive to this issue – product regulation, if done blindly, can damage the industry and harm, rather than help, the consumer. Consumer protection must be undertaken, therefore, as part of a comprehensive regulatory structure that looks at all aspects of the industry and its marketplace.

(3) Federal financial product oversight should be addressed only as part of a comprehensive review of insurance regulation.

To the extent you decide to include insurance products in a federal oversight scheme, it should be undertaken only as part of a broader effort to streamline and improve the current insurance regulatory regime. This should not be a piecemeal effort – as I have discussed above, the dangers and regulatory burdens are too great. If the federal government is going to assume insurance regulatory authority, there must be a federal insurance regulator with the expertise and authority to fully understand the implications of regulatory actions for the industry, the marketplace and consumers, and take action based on that knowledge.

We appreciate the Administration's call for the creation of an Office of National Insurance within the Treasury Department to serve as a federal source of expertise on insurance matters, and NAIFA was an early supporter of Rep. Kanjorski's Office of Insurance Information legislation. That is a welcome start for federal understanding of insurance. But an information-gathering office is not enough if the plan includes assumption of regulatory authority over insurance products. In that case, the federal government must fully understand the industry and be able to take appropriate and necessary regulatory actions so that product regulation meshes with, and does not conflict with, solvency and other substantive regulatory issues.

NAIFA members have debated long and hard regarding the proper federal role in insurance regulation. NAIFA members are long-time supporters of state regulation and remain steadfastly committed to this tradition. Having said that, NAIFA recognizes the shortcomings of the current regulatory structure. Unnecessary distinctions among the states and inconsistencies within the states on issues such as licensing, product approval, and consumer protection, thwart competition, reduce predictability and add unnecessary expenses to the cost of doing business, all of which ultimately harm consumers. We have – and continue to – work with the states to make improvements. We recognize that reform is critical to protect consumers and to ensure a strong and healthy insurance marketplace, and we believe that fixing the problems with the insurance regulatory system ultimately will enable the insurance industry to provide better and greater choices for consumers, without sacrificing consumer protection.

Despite the solid efforts made by the states to improve the current regulatory system, it has become increasingly clear that the state system needs help. NAIFA believes it is imperative that the problems and inefficiencies in the state regulatory system be corrected quickly, and supports the active involvement of the Congress in the reform process. To that end, NAIFA has had a policy in place since 2002 that supports in concept congressional action to improve and augment the regulation of insurance, provided such action meets NAIFA's specific guidelines aimed at maintaining fairness to agents and protection for the consumers they serve. To that end, NAIFA supports legislation introduced by Reps. David Scott and Randy Neugebauer, H.R.2554, which would create the National Association of Registered Agents and Brokers or "NARAB II" as it is frequently called. NARAB II would streamline the nonresident licensing requirements for agents choosing to do business in multiple states. NAIFA is also very supportive of an important consumer protection provision of NARAB II that would require all NARAB members to submit to a federal criminal background check – a requirement currently only imposed by only 17 states. We are incredibly thankful that this Committee approved NARAB II last Congress and it ultimately passed the full House in September of last year. H.R. 2554 has already received overwhelming support by the members of this Committee and we ask that you once again approve NARAB II and send it to the full House for their consideration.

With respect to comprehensive reforms, we specifically support the concept of an optional federal insurance regulator. To be clear, NAIFA's support for an optional federal insurance charter is not absolute. We continue to believe in the state system and recognize the benefits it offers for many insurance professionals and consumers. Moreover, no federal charter plan will gain NAIFA's support unless it meets the principles set forth by our members including, perhaps most important, the inclusion of strong consumer protections. (NAIFA's "Themes and Conditions for Support of the Concept of An Optional Federal Charter for Insurance" are attached hereto as Appendix A.)

NAIFA believes that federal charter legislation must provide a federal insurance regulator with authority to adequately address the following consumer protection issues:

a. Encompass the NAIC's model Unfair Trade and Unfair Claims Settlement Practices Acts;
b. Adhere to generally accepted replacement regulations;
c. Include file and use of rates with appropriate regulator review and approval of products;
d. Maintain the ability of insurers to share loss, underwriting and trending data;
e. Not exceed the 2004 NAIC standard for insurance commission disclosure;
f. Ensure adequate solvency standards for insurers; and
g. Include regulator responsiveness to and accessibility for consumers.

These principles are the guideposts for NAIFA's analysis and support of federal regulation of insurance. Strong consumer protections are essential to any workable federal oversight scheme. But, we believe they cannot be separated from other aspects of insurance oversight.

Conclusion:

The current financial crisis has rightly raised concerns about deficiencies in the regulatory oversight of certain types of financial products. The Obama Administration has proposed creating a new federal regulator, the Consumer Financial Protection Agency, to oversee those products and impose and enforce new rules with respect to the products and the people that provide them.

NAIFA has always supported strong consumer protections – it is good for our customers and good for us – and we fully understand the logic behind the Administration's proposal. Having said that, we strongly believe that insurance products should not be subject to federal product regulation unless it is undertaken as part of a comprehensive approach to insurance regulatory reform that addresses all issues related to insurance oversight including in particular solvency issues and the interaction with state laws and regulations.

We realize that this is the start of a long process toward improving our financial regulatory structure, and appreciate the opportunity to share our views with you today on this issue that is so critical to consumers and to our country. We welcome the opportunity to assist you in any way that we can as the legislative process moves forward.

Appendix A

NAIFA's Themes and Conditions for Support of the Concept of an Optional Federal Charter for Insurance

1. True Agent Choice

Federal insurance legislation shall:

a. Permit producers to choose federal or state regulation
b. Prohibit companies from discriminating against a producer based on his or her choice of federal or state regulation
c. Address producer regulation for all major lines of insurance

2. Enhanced Consumer Protections

Federal insurance legislation shall:

a. Encompass the NAIC's model Unfair Trade and Unfair Claims Settlement Practices Acts
b. Adhere to generally accepted replacement regulations
c. Include file and use of rates with appropriate regulator review and approval of products
d. Maintain ability of insurers to share loss, underwriting and trending data
e. Not exceed the 2004 NAIC standard for insurance commission disclosure
f. Ensure adequate solvency standards for insurers
g. Include regulator responsiveness and accessibility to consumers

3. Single Federal Voice & Preserve State Regulation

Federal insurance legislation shall:

a. Provide a single, comprehensive regulatory structure for all producers who opt for federal regulation
b. Include a federal entity with expertise in insurance to weigh in on national and international policy with regard to insurance
c. Provide producers with a position at the table when new regulations are being considered by the national insurance regulator
d. Allow for creation of a new self regulatory organization (SRO) to address insurance and/or securities issues
e. Allow for increased efficiencies and cost savings for our members
f. Create a federal insurance regulator who is the sole regulator of insurance for federally licensed entities -- not any other federal body
g. Be cost neutral to the states
h. Promote cooperation between state and federal regulators
i. Not impede the operation or expansion of the Interstate Insurance Product Regulation Commission (Interstate Compact) or other efforts to improve state insurance regulation
j. Fully preserve McCarran-Ferguson antitrust exemption for state regulation of insurance.