Testimony of the
National Association of Insurance Commissioners

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Committee on Financial Services
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Walter Bell
Alabama Commissioner of Insurance
President, National Association of Insurance Commissioners

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Introduction

Chairman Kanjorski, Congresswoman Pryce, and Members of the Subcommittee, thank you for inviting me to testify before the Committee on the need for insurance regulatory reform.

My name is Walter Bell. I am the Commissioner of Insurance in Alabama. I also currently serve as President of the National Association of Insurance Commissioners (NAIC). I am pleased to be here today on behalf of the NAIC and its members to update the Subcommittee on our ongoing, successful efforts to improve the state system of insurance supervision.

Having served as the front line of U.S. insurance regulation for over 150 years, state insurance officials have a record of consumer protection and industry oversight that is second to none. We take seriously our responsibility to ensure that the safety net of insurance is there when people need it. We have been a powerful advocate for insurance consumers, combining state-of-the-art databases and strong solvency regulation to ensure each and every consumer maximum protection. The current insurance regulatory scheme is strong, and equal if not superior, to the insurance regulatory schemes in place in other countries. State insurance regulators—along with other state and federal financial regulators who focus on fair tax treatment, improved corporate governance and increased transparency—work to produce a vibrant and competitive global marketplace for U.S. insurers.

Still, there are those who would claim an expanded federal presence is needed as an alternative to state consumer protections. They say a centralized authority that would offer deregulation to deal with a perceived "hodge-podge" of state governments and bring insurance regulation into the 21st Century. Mr. Chairman, Congresswoman Pryce, Members of the Subcommittee, I submit: State insurance regulation has been and continues to be a dynamic and robust success.

My testimony today will focus on state efforts to improve insurance regulation for U.S. consumers and industry. That has not occurred in a vacuum. The NAIC, and state insurance regulation in general, underwent serious review on Capitol Hill and in state legislatures in past decades. Major companies were going insolvent, policyholders were going unprotected, insurance scams were numerous, and state regulators—whether they deserved it or not—were seen to be asleep at the switch.

Congress held hearings—lots of hearings—detailing laxity and even corruption at the state level, criminals crossing state lines with impunity ("rascals and scoundrels," in the words of a once-and future Committee Chairman) and a regulatory scheme that appeared inconsistent at best, inept at worst.

The hearings culminated in two Committee reports that provided a permanent record of the perceived weaknesses of the state system of insurance regulation. They did not prove to be very pleasant reads for those tasked with overseeing the insurance industry and its various players, just as the allegations aired at the hearings were not easy to listen to.

But listen we did. And we acted.

State insurance regulation in 2007 is robust, effective and constantly evolving to better reflect the changing marketplace and better protect consumers. Where we may have been accused of being weak and passive fifteen or more years ago, we are today strong and effective.

I want to cover a number of major initiatives the NAIC has undertaken with state insurance regulators in recent years. We have been the face of regulatory reform, coupling an aggressive enforcement mindset with advanced techniques to provide comfort to American consumers in times of peril. My testimony will cover a number of major areas where we have taken the initiative and successfully strengthened the state insurance regulatory process.

- Speed to market;
- Solvency and guaranty funds;
- Consumer assistance and education;
- Fraud detection;
- Regulatory actions against companies, agents and brokers;
- Turnaround on rate and form filings;
- Producer licensing; and
- Company licensing.

Speed to Market

Insurance regulators have embarked on an ambitious "Speed to Market Initiative" that encompasses the following four main areas:

- Putting in place an interstate compact to develop uniform national product standards and provide a central point of filing ;
- Integrating multi-state regulatory procedures with individual state regulatory requirements;
- Encouraging states to adopt regulatory environments that place greater reliance on competition for commercial lines insurance products; and
- Making fully available a proactively evolving System for Electronic Rate and Form Filing ("SERFF") to achieve speed to market goals.

The Interstate Insurance Compact ("the Compact") is a key state-based initiative that allows insurers to file new life insurance, annuities and other wealth-protection insurance products and receive a single, streamlined review. This vital reform allows insurers to speed new products to market nationally according to strong uniform product standards, while preserving a state's ability to address front-line problems related to claims settlement, consumer complaints, and unfair and deceptive trade practices. States have embraced the Compact and have been speedily enacting it. To date, thirty states have implemented the Compact—representing half of U.S. nationwide premium volume—and more are in the process of doing so. It is worth noting that some of the states that have not yet joined the Compact have not been lobbied heavily to join because their product approval process is so rapid and efficient that it would be nearly impossible to improve.

The Compact created the Interstate Insurance Product Regulation Commission ("the IIPRC") when it met its threshold of 26 Member States and/or 40 percent of premium volume in May 2006. <u>It became fully operational earlier this year and reviewed and approved the initial filings in under thirty days - a dramatic demonstration of providing speed to market while upholding strong consumer protections.</u>

The uniform standards-setting process at the IIPRC is conducted through comprehensive public notice and comment periods that afford full opportunity for input to industry, consumers and the general public. The compact ensures that products can quickly enter the market while ensuring that those products have appropriate protections in place.

The NAIC has developed a set of uniform metrics based on the four operational efficiencies listed previously. SERFF already has the necessary accounting and reporting framework for both paper and electronic product filings, and has been implemented in all states.

Review standards checklists provide a means for insurance companies to verify the filing requirements of a state before making a rate or policy form filing. The checklists contain information regarding specific state statutes, regulations, bulletins or case law that pertain to insurance issues. Most states have developed and posted Review Standards Checklists to their state websites, which in turn may be accessed by all insurers through the NAIC's website. Insurers taking advantage of this regulatory modernization have found a dramatic increase in the likelihood for successfully submitting a filing, thus vastly improving speed to market.

The product requirements locator tool is available to assist insurers in locating the necessary requirements of various states when they are developing products for use in multiple states. Twenty-six states are using the property and casualty products requirement locator tool, with six more in the process of implementing it. Most jurisdictions are on pace to implement the life and health product requirements locator tool by the end of 2008.

The NAIC has developed product coding matrices to provide uniformity in naming and coding products. This will enable insurers across the country to communicate seamlessly with insurance regulators regarding product filings. To date, 33 states have implemented the Uniform Product Coding matrix within SERFF for all lines of business and an additional fifteen states are implemented for at least one line of business and working on full implementation.

The NAIC has developed Uniform Transmittal Documents to permit uniform product coding, so that insurers across the country can code their policy findings using a set of universal codes without regard to where the filing was made. The multiple codes developed historically by individual states for their own lines of insurance have been replaced by a set of common codes so that insurance companies no longer need to keep separate lists of codes. With the release of SERFF v5, to be discussed in a later section, 33 states have completely eliminated use of alternative transmittal documents and seventeen states have eliminated requirements for alternative transmittals for some lines of business and are working on elimination for all lines.

Solvency and Guaranty Funds

State insurance departments in the past fifteen years have continually enhanced their statutory authority and regulatory practices in this critical area. Major insurer insolvencies in the late ‘80s and early ‘90s, coupled with inadequacies in several state guaranty funds, stirred Congressional interest and led to cries for federal intervention. Due to action by state regulators, there has been a dramatic reduction in major insolvencies since that time.

Notable improvements by the state departments include:

- Codification of accounting practices into one comprehensive manual, resulting in consistent and comparable financial statements;
- Enhancement of financial reporting requirements on an annual and quarterly basis of key areas, including reinsurance, investments, reserves, significant disclosures and off-balance sheet risks;
- Refinement and development of analytical tools to provide state insurance regulators with an integrated approach to screening, prioritizing and analyzing the financial condition of insurers operating in their respective states;
- Strengthening of existing statutory authority, such as risk-based capital requirements, examination authority, investment regulations, reserving statutes, actuarial opinion guidelines, receivership and guaranty fund schemes and frameworks, and holding company considerations (including provisions regarding acquisition of control or merger);
- Enhancement of financial examination and analysis procedures and guidelines to be more risk-focused to better target resources and regulatory efforts; and
- Establishment of a more efficient company licensing process through the development and implementation of the Uniform Certificate of Authority application and an electronic tool for creating and submitting the applications.

Ultimately, these improvements have allowed regulators to identify more easily when insurers are troubled and react more quickly to protect policyholders and consumers.

Attachment 1 details more specifically the NAIC's efforts to continually improve the solvency framework used by all states.

Consumer Assistance and Education

With the many changes taking place in the financial services marketplace, consumer protection poses significant challenges to a regulator. I am happy to say that state insurance regulators have risen to the challenge. Insurance is a unique and complex product that is fundamentally different from other financial services, such as banking and securities. Unlike banking products, which provide individuals up-front credit to obtain a mortgage or make purchases, or securities, which offer investors a share of a tangible asset, insurance products require policyholders to pay premiums in exchange for a legal promise. Insurance is a financial guarantee to pay benefits, often years into the future, in the event of unexpected or unavoidable loss that can cripple the lives of individuals, families and businesses. The cost to insurers to provide those benefits is based on a number of factors, many of which are prospective assumptions, making it difficult for consumers to understand or anticipate a reasonable price. Unlike most banking and securities products, consumers are often *required* to purchase insurance both for personal financial responsibility and for economic stability for lenders, creditors, and other individuals. Insurance products are bathed in the public interest and responsibility; they inevitably touch a host of important and difficult issues whose impact is felt locally. Most consumers find themselves concerned with their insurance coverage, or lack thereof, only in times of crisis—such as illness, death, accident or catastrophe. State officials have responded quickly and fashioned effective remedies to respond to local conditions in the areas of claims-handling, underwriting, pricing and market practices.

The NAIC provides a forum for education and information exchange, with more than 64 courses on a variety of insurance topics, and eighteen programs designed specifically for insurance regulators. In 2006, the NAIC launched the Insurance Regulator Professional Designation Program to enhance regulators' skills, techniques and strategies for monitoring the insurance marketplace.

The NAIC has been proactive in ensuring that state insurance regulators have the very latest and best tools to educate consumers on important insurance issues. These have included outreach campaigns, public service announcements and media toolkits. With its landmark *Insure U—Get Smart about Insurance* public education program, (www.insureuonline.org) the NAIC has demonstrated its deep commitment to educating the public about insurance and consumer protection issues. Insure U's educational curriculum helps consumers evaluate insurance options to meet different life stage needs. Available in English and Spanish, the Insure U website covers basic information on the major types of insurance—life, health, auto and homeowners/renters insurance. It also offers tips for saving money and selecting coverage for young singles, young families, established families and seniors/empty nesters. There is a quiz for each life stage, enabling consumers to test their knowledge on insurance issues and topics. We have produced a new TV public service announcement, tailored to each state and providing contact information for the state insurance department, warning consumers how to protect themselves from fraudulent insurance schemes. Consumers may also call a toll-free telephone number to find consumer representatives in their home state insurance departments. Already, more than forty stories about Insure U have been carried by AP, Reuters, UPI, The Wall Street Journal, The Washington Post blog, the Atlanta Journal Constitution, The Chicago Tribune, The New York Daily News, and various other newspapers. Additionally, eleven radio interviews on Insure U aired on CNN radio and local stations in Connecticut, California, Missouri and Arizona, reaching over a million listeners in that medium alone. Collectively, Insure-U's public outreach has registered 158 million media impressions.

Fraud Detection

In January 2005, the NAIC launched an online fraud reporting mechanism to allow consumers, employees, or others who suspect wrongdoing to report their suspicions anonymously to state enforcement authorities. Since business practices in one state may be connected to problems in other states, the system allows for focused fraud detection in close proximity to where problems arise. Continued regulatory collaboration avoids duplicative and excessive data requests that delay responses from the producer and insurer industries and hinder appropriate state regulatory action.

Regulatory Actions Against Companies, Agents and Brokers

Although not law enforcement agents in most states, state regulators do effectively prevent unfair trade practices as part of their supervisory authority. Every state has laws in place to address unfair trade practices, giving the insurance regulator ultimate authority to investigate a variety of unfair practices, impose fines and require appropriate corrective actions. For example, the Trade Practices Law in my state of Alabama prohibits unfair methods of competition as well as unfair or deceptive acts in the business of insurance, including benefits, unfair claims handling procedures and other fraudulent practices.

State regulators' primary responsibility is to maintain the stability of insurance markets and products for the benefit of consumers. Conscientious and highly skilled regulatory professionals monitor the business activities of insurers every day to assure that the companies have the financial wherewithal to make good on their promises and treat their policyholders and claimants fairly.

State insurance officials actively supervise insurers' market conduct through market analysis, periodic examinations and investigation of specific consumer complaints. Consumers having problems with their homeowners, health, automobile or life insurance can readily contact state insurance regulators by email, telephone, regular mail and personal visits. State regulators earn consumer trust because they know the cities, towns and communities where consumers live, as well as the nuances of the local insurance marketplace.

Insurance products are complex financial instruments, and therefore difficult for many consumers to understand. Working together, regulators and responsible business participants help to strengthen financial stability and fairness in the marketplace. State insurance regulators' extensive daily monitoring of solvency, review of rates and policy forms, and evaluations of market behavior, coupled with state attorneys general enforcement of state antitrust laws, have produced a vigorous and active insurance regulatory scheme providing maximum consumer protection.

Given their primary role in the protection of insurance consumers, state insurance commissioners take pride in the historical fact that state-based regulation works very well to provide consumers with a healthy marketplace and confidence that the basic obligations set forth in their insurance policies will be met. When the marketplace functions without significant problems, it means that we are working successfully to protect consumers by maintaining competitive and stable insurance markets.

A recent example demonstrates this well. Following more than a year of analysis by the New York Insurance Department, the state attorney general's office in October 2004, obtained a number of indictments and guilty pleas against a large brokerage firm for bid-rigging and other fraudulent activities.

The system of active state insurance supervision worked. Existing state consumer protection, antitrust and unfair trade practice laws provide the necessary tools and enforcement mechanisms to stop anticompetitive conduct. Without admitting or denying the allegations against them, several of the nation's top brokerage firms and major insurers entered into consent agreements with a number of attorney generals and state insurance departments. The agreements establish settlement funds ranging from $2 million to $850 million, from which payments were made available to policyholders.

For a more detailed review of state and NAIC actions regarding antitrust violations related to producer compensation, please refer to Attachment 2.

Turnaround on Rate and Form Filings

The NAIC's System for Electronic Rate and Form Filing ("SERFF") provides a single point of filing for insurance products, and is the filing system used by the IIPRC. Insurers choosing SERFF to file their products experience a considerably shorter turnaround time for the entire filing submission and review cycle than is possible under the traditional paper filing process. Some SERFF filings are turned around in a single day. SERFF is currently being used by all fifty states, the District of Columbia, Puerto Rico and over 2,600 insurance companies. Insurers' use of SERFF has grown tremendously in the last five years, with more than 270,000 filings submitted for review and approval during 2006.

Late last year the NAIC released SERFF v5, unveiling new functionality and expanded filing options. Following this release, eleven states have mandated, or announced plans to mandate, the use of SERFF, and more states are considering doing so. As mentioned earlier, SERFF v5 has succeeded in making the Uniform Transmittal Documents accessible to all jurisdictions.

Producer Licensing

By developing and utilizing electronic applications and databases, state insurance officials have created much greater efficiencies in licensing and appointing insurance producers in those states that require it. State insurance officials remain deeply committed to achieving greater uniformity in the producer licensing process, demonstrated by the Standard Uniform Producer Licensing Application now used in every state. An overwhelming majority of states now accept non-resident licensing applications electronically.

The National Insurance Producer Registry (NIPR) is governed by a 13 member board of directors that includes state regulators and industry. NIPR developed and implemented the Producer Database (PDB) and Electronic Appointments/Terminations.

The PDB is a state of the art electronic database that links state regulatory licensing systems into one common repository of producer information. The PDB also includes data from the Regulatory Information Retrieval System (RIRS) to provide a more comprehensive producer profile. The key benefits of PDB are:

- Financial/Time Savings
- Reduction in Paperwork
- Real Time Information
- Verify License and Status in All Participating States
- Ease of Access via the Internet
- Single Source of Data vs. Multiple Web Sites

The NIPR Gateway is a communication network that links state insurance regulators with the entities they regulate to facilitate the electronic exchange of producer information. Data standards have been developed for the exchange of license application, license renewal, appointment and termination information. The key benefits of NIPR Gateway are:

- Reduction in paperwork and data entry
- Development of national standards regarding electronic transmission of licensing data
- Faster turnaround time

The NAIC has formed a Producer Licensing Coalition to create a partnership of state regulators and national producer trade associations to fully implement national uniform producer licensing standards. While the NAIC has made great progress in implementing these standards over the past few years, we think it is time for the producer trade organizations to make a stronger contribution, such as:

- Finalizing agreement on what our uniform licensing standards should look like and promoting their implementation nationwide; and
- Developing national professional producer standards intended to help producers "walk the talk" in representing themselves as professionals in serving the needs of insurance consumers across the country.

We are also embarking upon a national self-assessment of the states continued compliance with the reciprocity provisions of the Gramm-Leach-Bliley Act, as well as measure our progress and identify any barriers to full implementation of the national uniform licensing standards developed by the NAIC. By performing on-site reviews of state producer licensing functions, we will validate these processes are working as intended, identify any areas for improvement, and document best practices for incorporation into a national handbook.

Company Licensing

To simplify insurers' application process for state licenses to write insurance, the NAIC has developed a Uniform Certificate of Authority Application ("UCAA"), an electronic system designed to help navigate state-specific requirements. We will continue to leverage information technologies and rethink our processes to make business expansion more efficient, while keeping our focus on protecting consumers from rogue insurance management.

Insurance: A Unique Financial Product that is Regulated Effectively by the States

Paying for insurance products is one of the largest consumer expenditures of any kind for most Americans. An average family easily can spend over $7,000 each year for auto, home, life, and health insurance coverage. This substantial expenditure—often required by state law or business practice—is typically much higher for families with several members, more than one car, or additional property to insure. Consumers clearly have an enormous financial and personal stake in making sure that insurers keep their promises.

Insurance is based upon a series of subjective business decisions, many local rather than national in scope: Where does the policyholder reside? Is the insured property subject to earthquakes or hurricanes? How close is the nearest fire department? What is the policyholder's risk of civil liability under the laws of the state? Will an insurance policy be offered to a consumer? At what price? What are the policy terms and conditions? What is the structure of the local hospital and physician marketplace? All of these subjective business decisions add up to one absolute certainty: Insurance products can generate a high level of consumer backlash and customer dissatisfaction that in turn requires a high level of regulatory expertise, accountability and responsiveness.

Every day, state insurance departments make certain that insurers meet the reasonable expectations of American consumers, including those who are elderly or low-income, with respect to financial safety and fair treatment. In 2006, state insurance departments handled approximately three million consumer inquiries and complaints nationwide, many of which were resolved successfully at no cost to the consumer. The states also maintain a system of financial guaranty associations that cover policyholder losses in the event of an insurer insolvency. The entire state insurance system is authorized, funded, and operated at absolutely no cost to the federal government.

States Oversee a Vibrant, Competitive Insurance Marketplace

In addition to successfully protecting consumers, state insurance officials have proven adept stewards of a vibrant, competitive insurance marketplace. The insurance industry in the United States has grown exponentially in recent decades in terms of the amount and variety of insurance products and the number of insurers. In 2006, there were 7,660 domestic insurers operating in the United States (an increase of more than 1,000 companies from 2004), with a combined premium of $1.409 trillion. As a share of the U.S. economy, total insurance income grew from 7.4 percent of gross domestic product in 1960 to 11.9 percent in 2000. In 2005, while insurance companies were absorbing record losses, they were also making record profits. Profits and surplus increased again in 2006, and the industry is on pace to set yet another record this year. Insurance company surplus is now over $500 billion for the first time ever.

Although these national numbers reflect a large industry, most insurers and most of the nation's four million insurance agents and brokers operate in three or fewer states. Even the giants of the industry use slogans that imply a close-knit local flavor such as "Like a good neighbor" or

"You're in good hands."

Today, companies of various sizes sell a vast array of products across state and national boundaries, reflecting the growing national economy and diversity of buyer needs, and the demand for insurance protection and investment products. Industry changes caused regulatory institutions to evolve, and state supervisory evolution, in turn, has contributed to the development of the insurance industry. This has resulted in a nimble regulatory environment that clearly has served insurance consumers well.

Insurance Regulatory Modernization: A Dynamic Process

Insurance supervision in recent years has been subject to increasing external and internal forces, to which the states have responded. Fundamental changes in the structure and performance of the insurance industry have complicated the challenge. Competitive forces have caused insurers to assume increased risk in order to offer more attractively priced products to consumers. Insurance companies have become increasingly national and international in scope and have widened the boundaries of their operations. One constant, however, remains: Insurance markets and the perils consumers face remain uniquely local.

A singular U.S. market for property, auto and many other lines of insurance business does not exist. Each state, and in some cases, even each zip code, represents a distinct market, with varying risks, products and prices. Tort laws, court systems, workers' compensation laws and the perils for which individuals and businesses buy insurance differ widely from state to state. Unlike the federal government, states have acted quickly and decisively after recent natural disasters, ranging from the Gulf Coast hurricanes to wildfires in the West, and tailored their responses to the challenges of their particular states.

When state insurance markets are compared to other national insurance markets around the globe, the size and scope of those states' markets—and therefore the responsibility of state regulators—typically dwarfs the markets of whole nations (see attachment 3). Four of the top ten and twenty-six of the top fifty insurance markets in the world are U.S. states. For example, Mr. Chairman, the insurance market in your home state of Pennsylvania is larger than the insurance market in China. Likewise, the markets in Ohio and Michigan are larger than the markets in India, Ireland or South Africa. The market in Tennessee is larger than the market in Russia or Denmark. Each of these markets demands a local, accountable, and responsive regulator.

The insurance industry today is driven by individuals and families dealing with a local insurance agent to provide coverage for homes and autos, health care from local providers, whole and term life insurance products to protect young families against the economic devastation caused by the premature death of a breadwinner, and annuities and other investments to help fund a college education or retirement.

The convergence of forces has had a dramatic effect on the supervision of insurance. Over the past two decades, the states have engaged in an unprecedented program to revamp the framework of insurance oversight. Insurance officials have worked continuously to upgrade the state system to provide multi-state platforms and uniform applications to leverage technology and enhance operational efficiencies. A good share of this effort in the late 1980s and 1990s was directed at strengthening financial oversight by establishing higher capital standards for insurers, expanding financial reporting, improving monitoring tools and accrediting insurance departments. Subsequent initiatives have focused on improving the effectiveness and efficiency of product regulation, market surveillance, producer licensing, company licensing and general consumer protections.

The states have enhanced the resources devoted to insurance supervision, and the NAIC through its members has played a central role in state efforts to strengthen and streamline oversight of the insurance industry. These are not one-time silver bullet solutions, but rather represent a dynamic, ongoing process that changes and evolves along with the business of insurance that we oversee. The modern system of insurance supervision builds on over 150 years as stewards of a healthy, vibrant insurance marketplace founded upon a bedrock of comprehensive policyholder and consumer protection. But it also demands that state insurance officials be ever vigilant and nimble to anticipate and respond to the changing needs of consumers, the industry and the modern marketplace.

Modernize, Don’t Federalize

As states have moved forward to modernize insurance supervision, Congress has begun to consider federal legislation related to insurance regulation. The NAIC and its members welcome Congressional interest in insurance supervision. At the same time, we urge careful analysis of any proposal to achieve modernization of insurance supervision through federal legislation. Even well intended and seemingly benign federal legislation can have a substantial adverse impact on existing state protections for insurance consumers. One of the great strengths of state insurance regulation is the fact it is rooted in other state laws that apply when insurable events occur. Federal laws that appear simple on their face can have devastating consequences by limiting the ability of state insurance departments to protect the public.

Proponents of efforts to federalize the regulation of insurance use buzz words such as "uniformity," "modernization" and "streamlining"—all of which have been at the heart of the NAIC's successful efforts to strengthen the state regulatory process. Another familiar theme for the pro-federalization crowd is "deregulation," a concept that may sound appealing at first blush but in reality is fraught with peril. For what they are really talking about is *deregulating consumer protections*. Mr. Chairman, Congresswoman Pryce, Members of the Subcommittee, I would dare say that not one of your constituents would favor that—unless, that is, they are affiliated with an insurance company.

There are limited areas where insurance regulation could benefit from a federal presence. Note that I say *presence*, not *takeover* or *preemption*.

State insurance regulators have long been hampered by their inability to gain access to FBI background checks that may exist for potential insurance agents or brokers. We are committed to keeping the "rascals and scoundrels" out of our business, but we should have the same tools as other financial regulators in order to do our jobs as effectively as possible.

Certain catastrophes can be national in scope, overwhelming the ability of states and the private markets to handle them. The terrorist attacks on September eleventh are a good example, and indeed spawned the TRIA legislation that provides a federal insurance backstop in the event of a terrorist attack. A mega-natural disaster could well have the same effect—say, a large hurricane striking the Hudson River Valley or Long Island, or a major earthquake occurring along the New Madrid fault.

The federal government does not have a stellar record when it takes wholesale control of sectors of the insurance industry. Federal preemption of state regulation in the Medicare Advantage market in 2003 has caused numerous problems for consumers. Senior citizens have been victimized by abusive practices, including misrepresentation, deceptive or inappropriate sales practices, and in many instances, fraud. In Georgia, special agents for the state's insurance commissioner found that insurance agents had signed up *deceased* individuals prior to the enrollment period using the deceased individual's personal information retrieved from insurance agency databases and Medicare Part D applications. North Carolina insurance investigations revealed cases of insurance agents who had switched residents of an assisted living community from traditional Medicare into private plans without their permission.

In the absence of the federal preemption imposed by the Medicare Prescription Drug Improvement Act, many of these abusive practices would be prohibited by state law, monitored and questioned by watchful state regulators and controlled by the state regulatory structure. However, since these cases involve Medicare Advantage, or Part D, plans, the hands of state regulators are largely tied. The marketing guidelines are established by the federal government, states are largely prohibited from monitoring the marketplace and states have very limited ability to take corrective action against a company for misconduct. It has unfortunately become evident to states, lawmakers and consumer advocates that the federal government does not have the expertise nor the manpower to adequately protect consumers in this area.

In sharp contrast, Medicare Supplement (Medigap) insurance, which is monitored by effective state regulation, sees relatively few consumer complaints and no such widespread problems, even though it serves a similar population and is sold to seniors in a similar manner. In fact, several Congressional Committees are now looking to the state regulation of Medicare Supplement insurance as a potential template for remedying the problems with Medicare Advantage and part D plans.

Conclusion

The system of state insurance supervision in the United States has worked well and has continuously evolved for over 150 years. State regulators understand that protecting America's insurance consumers is our first responsibility. We also understand that commercial insurance markets have changed, and that modernization of state insurance standards and procedures is needed to facilitate more streamlined, harmonized and efficient regulatory compliance for insurers and producers.

The NAIC and its members—representing the citizens, taxpayers, and governments of all fifty states, the District of Columbia and U.S. territories—will continue to share our expertise with Congress on insurance issues having a national impact and welcome Congressional interest in our modernization efforts. We respectfully request Congress and insurance industry participants to work with us to continue to modernize insurance regulation and protect consumers. As our tremendous progress to date shows, that is the only practical, workable way to maintain the strong protections consumers demand—and deserve.

Insurance consumers require a financially sound and secure insurance marketplace that offers a variety of products and services. They have that now through an effective and responsive state regulatory system. Putting our record of success up against the uncertainties engendered by changing to a federal system is a losing bet. A nimble state-based system that works well at no cost to the federal government is far preferable to a one-size-fits-all federal regulatory scheme. When you look at the tradeoffs, we believe that you in the Congress will agree that insurance regulation is best left to home state officials with the expertise, resources, and experience to protect consumers in the communities where they live. Thank you for this opportunity to address you, and I look forward to your questions.

ATTACHMENT 1

State Insurance Departments' Continuous Improvement to the Solvency Framework

The state insurance department's solvency framework provides crucial safeguards for the United State's insurance consumers. This solvency framework includes all aspects of a potential insurer life cycle, including licensing, monitoring (i.e. financial reporting, financial analysis and examination), supervision/receivership and guaranty fund aspects. In order to ensure the effectiveness of the solvency framework, the state insurance departments over the past fifteen years have continually enhanced statutory authority and regulatory practices, including participation in the NAIC Financial Regulation Standards and Accreditation Program, which establishes baseline requirements in each state.

Notable enhancements by the state insurance departments over the last few years are as follows:

- Codification of accounting practices into one comprehensive manual, resulting in consistent and comparable financial statements;

- Enhanced financial reporting requirements on an annual and quarterly basis of key areas, including reinsurance, investments, reserves, significant disclosures, off-balance sheet risks, etc.;

  - The quality of insurer financial statements continues to benefit from the codification of statutory accounting principles and the state regulatory system of refining and improving instructions for statutory financial statements. While the number of companies filing with the NAIC have increased from 5,019 in 2004 to 5,083 in 2006, and the number of data quality consistency validations applied to each filing have increased as well, the number of errors generated from these validations have decreased from 12,111 in 2004 to 9,856 in 2006.

- Refinement and new development of the collection of regulator only analytical tools designed to provide state insurance departments with an integrated approach to screening, prioritizing and analyzing the financial condition of insurers operating in their respective states;

  - The significant use and refinement of analytical tools has steadily increased over the years from approximately 193,000 hits during 2001 to over 252,000 hits during 2006. The significant number of hits to these analytical tools demonstrates the number of useful tools available to regulators to analyze insurers in the most efficient manner. The increase in utilization demonstrates regulators constant attempt to improve their process through the development and use of additional tools.

- Strengthening existing statutory authority, such as risk-based capital requirements, examination authority, investment regulations, reserving statutes, actuarial opinion guidelines, receivership and guaranty fund schemes and frameworks, holding company considerations, including provisions regarding acquisition of control or merger;

  - As noted, these changes have strengthened statutory authority, and have helped regulators in their overall protection of insurance consumers. Some of these changes have been easily noticed, such as the increase in the level of capitalization in the HMO industry. In 1998, HMOs were required to complete the NAIC RBC formula for the first time, and the number of companies triggering an RBC action level has been reduced by 71% from 1998 to 2006, to only 34 companies. The life and property/casualty industry has generally been well capitalized, and the number of companies within an RBC action level for those industries has remained small at under 3% from 1994-2006.

- Enhanced financial examination and analysis procedures outlined in state insurance regulator handbooks and guidelines to be more risk focused in order to better target resources and regulatory efforts;

    - Early state adopters of the enhanced financial examination approach have developed a closer regulatory relationship with their domestic insurers, and in one case witnessed a dramatic reduction in examination costs; and

- Established a more efficient company licensing process through the development and implementation of the Uniform Certificate of Authority Application (UCAA) and an electronic tool for creating and submitting the applications.

    - Refinements in the UCAA processes and establishing best practices for regulatory reviews have reduced the average response time for UCAA applications from 174 days in 2005 to 55 days in 2007.

Ultimately, these accomplishments have allowed regulators to more easily identify troubled insurers and react in a manner that is in the best interest of policyholders and consumers.

- This fact can be illustrated by the decrease in the amount of correspondence that key regulators of multi-state companies have had to initiate with domiciliary states of troubled companies. More specifically, during the period 1992-1996, this type of communication with domiciliary states was necessary for 35% of potentially troubled companies. The following five years (1997-2001) this percentage decreased to approximately 30%, and the following five years (2002-2006), the percentage has decreased further to approximately 24%.

While some of this has to be attributed to the market cycle, it is also indicative of improved solvency regulation. Additionally, evidence exists to illustrate that the number of insolvencies has reduced over the last 10 years.

- This fact has been illustrated by information produced for public display by AM Best Rating agency. In March 2007, AM Best issued reports that showed how insurance impairments (which the report indicates is broader than insolvencies), have decreased from a five year high of approximately 97 per year through the years 1987-1991, to approximately 53 per year through the years 1992-1996, or approximately a 45% decrease. The same low level of impairments continued from 1997-2001, but has decreased even further during 2002-2006, where impairments are down 26% to approximately 39 per year. This public information is consistent with NAIC data, and in particular, the last five years indicates that insolvencies have decreased to 22 in 2001, and have steadily decreased to only 6 in 2006.

ATTACHMENT 2

State and NAIC Actions Regarding Producer Compensation Issues

In October 2004, the State of New York brought antitrust charges against a large insurance brokerage, stemming from contractual and implied arrangements between insurers and producers in which the insurer pays extra commissions to the producer based on a number of factors, such as the loss ratio or retention of business placed through the brokerage firm. These commissions were in addition to the regular, or "base," sales commission, and were often based on the performance of the insurer's entire book of business with an individual producer. Although these types of contingent commissions have been commonplace for more than a century, certain producers and carriers "rigged" the competition. For example, a producer would steer a particular piece of business to one insurer based on a favorable commission structure. In some cases other insurers participated by offering less-attractive prices, called "B quotes," to steer a policyholder to the pre-selected insurer. Producers also froze out insurers with less favorable commission arrangements, regardless of whether the insurers fit a customer's needs. In no uncertain terms, for both law enforcement and insurance regulation, this conduct constituted fraud, an unfair business practice, and a violation of state antitrust law.

When the original allegations surfaced in October 2004, the NAIC also appointed a task force to quickly develop a three-pronged national plan to coordinate multi-state action on broker compensation issues. The first prong of the NAIC's national action plan was to amend its existing Producer Licensing Model Act to require greater transparency of producer compensation in certain circumstances. The NAIC followed an accelerated time frame, adopting the amendment in December 2004 in order to have it available for 2005 state legislative sessions. The NAIC model disclosure amendment focuses on consumer protection. The amendment does not prohibit payment of contingent commissions or restrict the ability of producers to receive appropriate compensation for provided services. Instead, insurance agents and brokers are required to disclose the existence and certain terms of compensation arrangements, which in turn allows consumers to make informed choices. This approach respects business realities and market-driven forces, while at the same time prioritizing consumer protection. To date, seven states have adopted all or part of the reforms in the NAIC amendment, and others are considering them. Four more states have issued bulletins. These measures are in addition to existing statutory limitations or related disclosure regulations already on the books in many states. For example, one state barred contingent commissions in the mid-1980s. Also, by virtue of numerous settlements with brokers and carriers, written disclosure is becoming an effective industry standard.

The second prong of the NAIC's national action plan was to facilitate consistent regulatory action among the states, starting with the distribution of uniform templates for states to use in investigating producer compensation issues. Based upon the findings and monetary relief produced by the New York Insurance Department's settlement with Marsh & McLennan, the nation's largest producer, the NAIC's Broker Activities Task Force coordinated a multi-state regulatory settlement that has been joined by at least 32 other insurance departments. In exchange for releasing related regulatory claims, the signatory regulators can enforce the settlement's terms locally and receive compliance reports directly from Marsh & McLennan, while maintaining state-based ability to continue ongoing investigations. The Task Force released a similar settlement with the nation's second largest broker, Aon Corporation, which has garnered 28 signatory states. The Task Force is currently working on similar multi-state agreements with other large national producers. In addition, regulatory staff from six states, together with attorneys general from ten states reached a settlement with insurer Zurich North America arising out of bid-rigging allegations and resulting in $151 million in restitution to Zurich policyholders. The Zurich regulatory settlement has been adopted by fifteen chief insurance regulators to date. The Task Force has now wrapped up its work but the NAIC and its members will continue with collaborative efforts to reach settlement agreements with other producers and commercial insurance carriers, where appropriate and in conjunction with domestic regulators.

The third prong of this action plan is the development of the Online Fraud Reporting Mechanism discussed at page 8 of our testimony.

Attachment 3

Premium Volume -- Worldwide

Rank	Jurisdiction	Premium Volume	Market	Rank	Jurisdiction	Premium Volume	Market
		(In Millions US $	Share			(In Millions US $	Share
1	Japan	$460,261	11.48%	26	Massachusetts	$39,668	0.99%
2	United Kingdom	$418,366	10.43%	27	Belgium	$37,889	0.94%
3	France	$251,164	6.26%	28	Georgia (USA)	$36,065	0.90%
4	Germany	$204,544	5.10%	29	Virginia	$35,548	0.89%
5	Italy	$138,679	3.46%	30	North Carolina	$35,127	0.88%
6	California	$131,366	3.28%	31	Maryland	$31,041	0.77%
7	New York	$127,596	3.18%	32	Connecticut	$30,860	0.77%
8	Florida	$101,704	2.54%	33	Brazil	$30,390	0.76%
9	South Korea	$101,179	2.52%	34	Sweden	$29,182	0.73%
10	Texas	$91,015	2.27%	35	Washington	$28,975	0.72%
11	Canada	$88,200	2.20%	36	Minnesota	$28,544	0.71%
12	Pennsylvania	$75,441	1.88%	37	Wisconsin	$28,402	0.71%
13	PR China	$70,805	1.77%	38	Missouri	$27,270	0.68%
14	Spain	$65,813	1.64%	39	Indiana	$26,233	0.65%
15	Netherlands	$62,669	1.56%	40	Colorado	$25,441	0.63%
16	New Jersey	$62,201	1.55%	41	Arizona	$25,350	0.63%
17	Illinois	$59,417	1.48%	42	Delaware	$24,779	0.62%
18	Australia	$52,561	1.31%	43	Tennessee	$24,345	0.61%
19	Taiwan	$51,562	1.29%	44	Denmark	$23,262	0.58%
20	Michigan	$50,027	1.25%	45	Russia	$21,504	0.54%
21	Ohio	$49,627	1.24%	46	Hong Kong	$19,842	0.49%
22	Ireland	$47,281	1.18%	47	Louisiana	$19,695	0.49%
23	India	$43,032	1.07%	48	Austria	$19,568	0.49%
24	Switzerland	$41,758	1.04%	49	Finland	$19,308	0.48%
25	South Africa	$40,731	1.02%	50	Oregon	$17,983	0.45%
	All the Rest	$436,338	10.88%				
	Worldwide Total	$4,009,608	100.00%				
Sources: NAIC Financial Database for USA							
and SwissRe Sigma No. 4/2007 for the remainder.							