



STATEMENT OF
THE AMERICAN COUNCIL OF LIFE INSURERS
BEFORE THE
COMMITTEE ON FINANCIAL SERVICES
OF THE
UNITED STATES HOUSE OF REPRESENTATIVES
ON
THE FEDERAL INSURANCE OFFICE

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Statement Made by
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Mr. Chairman, Ranking Member Bachus and members of the Committee, my name is Dennis Herchel and I am Assistant Vice President and Counsel for Massachusetts Mutual Life Insurance Company. I am here today on behalf of the American Council of Life Insurers (ACLI), the principal trade association for U.S. life insurance companies. The ACLI's 340 member companies account for approximately 93% of the industry's total assets, 94% of the industry's domestic life insurance premiums and 94% of its domestic annuity considerations.

I appreciate the opportunity to appear before you today to share our views on the proposed substitute amendment to H.R. 2609, which would create the Federal Insurance Office (FIO) within the Department of the Treasury. This amendment, based largely on a proposal circulated earlier this summer by the Administration, is a proposal the ACLI strongly supports. In fact, given the breadth of the Administration's proposed response to the financial crisis and the applicability of that response to insurers, we believe it is imperative that the status and role of the FIO within the federal systemic risk regime be strengthened beyond what has been proposed. Doing so will ensure that insurance industry issues are given parity of consideration and importance by the systemic risk regulator to that given to issues affecting other financial industry sectors if broader reform is enacted. Our testimony today will focus both on possible changes to the proposal we believe can achieve that goal, as well as amendments that we think will improve the role of the FIO as originally envisioned.

We support the FIO for many of the same reasons we have supported past proposals to create the Office of Insurance Information, both this year and in 2008. Then as now, we believe the FIO would be enormously beneficial to Congress as it considers issues that are vitally important to our business; would facilitate the handling of international insurance matters; and would provide a means for

effectively involving the insurance industry as national policy decisions are made affecting U.S. financial institutions.

The events of the past 12 months have only served to strengthen the arguments for creating this Office. The financial crisis has all too clearly illustrated the problems associated with the lack of insurance industry expertise at the federal level. As you know, for some time now the ACLI has advocated for the creation of a federal regulatory presence, in the form of an optional federal charter, as the best way to modernize U.S. insurance regulation while also filling the federal government's gap in insurance industry knowledge and expertise. In light of the recent crisis and the various legislative proposals in response, and short of Congressional action creating a federal insurance regulator, we believe it is imperative that Congress act now to establish the FIO.

As proposed, the FIO would effectively serve two roles: it would be the federal government's repository of insurance industry information and expertise and also act as the United States' international representative on insurance issues. It would not have any supervisory or regulatory authority over any insurer doing business in the U.S. In addition to these parameters, which we support and will discuss further below, we believe the FIO should be elevated in status so that it can participate actively and effectively with federal financial industry regulators, including a systemic risk regulator, under any new systemic risk regulatory paradigm that may be implemented. Doing so will ensure that actions and decisions affecting insurers are taken only after any proposed systemic risk regulator has had direct consultation and coordination with the FIO. Given the lack of federal insurance industry expertise today, we believe this role is a critical one for the FIO to fulfill.

The Administration's systemic risk regulation proposal places the Federal Reserve Board (Board) in the position of ultimate systemic risk regulator. As such, the Board would be given broad authority to determine which companies pose "systemic risk", designate them as "Tier 1 Financial Holding Companies", and exercise broad prudential regulatory powers over Tier 1 companies and all of their subsidiaries. This authority would include the power to require increased capitalization or changes in management activities. This power is tempered only slightly, as the Board is required to consult and coordinate with the federal functional regulator of a Tier 1 company or its subsidiary before instituting any supervisory action or enforcement proceeding against it. However, since there is no federal functional insurance regulator, there would be no equivalent consultation or coordination when it comes to Board decisions affecting insurers that are either designated Tier 1 or are subsidiaries of a Tier 1.

Given that the Board is purely a banking regulator and has no insurance regulatory expertise, we believe this result to be highly inappropriate and is potentially damaging to insurers and their customers. The Board would be required to coordinate with other banking regulators, even though it has strong expertise in that area. However, the fact that it would not be required to act similarly when it comes to another major financial industry -- with which it has virtually no regulatory experience -- is an unacceptable contradiction of sound regulatory policy. From our perspective, this glaring oversight reinforces our concerns with the federal government's lack of understanding of the insurance industry (a concern magnified by the fact that the Administration's new Bank Holding Company Act proposal inexplicably fails to include insurance companies altogether in its statutory list of "functionally regulated subsidiaries"). Insurance is a highly regulated industry, where companies who do business in more than one state are supervised by a functional regulator in each of those jurisdictions. Insurance companies are subject to a strict financial solvency regime. Establishing

a systemic risk regulatory system that ignores these facts is an imprudent approach for the federal government to take, and is likely to result in unintended negative consequences for the industry, its customers and the economy.

We believe one solution to this problem is to give the FIO a role equivalent to that of federal functional regulators when it comes to dealing with the Board on all aspects of systemic risk regulation. For example, the Board should be required to coordinate and consult with the FIO whenever a Board supervisory or enforcement action is directed at an insurer in the same way and to the same degree it is required to do so with federal functional regulators of other entities. The FIO should be required to act as intermediary between the Board and an insurer's domestic state regulator regarding any proposed Board action. And the FIO should be given a seat on the proposed Financial Services Oversight Council so that the Council is constantly and contemporaneously made aware of relevant insurance industry issues. These and other changes in the FIO's status as to its relationship to the systemic risk regulator will help address insurer concerns and vastly improve whatever systemic risk regulatory regime is ultimately enacted by Congress.

In addition to these parity issues, we believe the proposal should be amended in a number of ways which, we believe, help strengthen and effectuate the role originally envisioned for the Office. First, we would not want to see the FIO's preemption authority in relation to international agreements employed in a way that leads to a real or potential regulatory "solvency gap." We do believe there may be circumstances under which the FIO can appropriately use preemption to advance sound international insurance policies without giving rise to such a gap, but any enacted language must make clear that such situations are the only circumstances when this power could be used. Also, we would not want to see preemption result in any material, unfair discrimination against any U.S. insurer.

While we do not believe use of preemption should be withheld if it can be used to realize the benefits provided under mutual or unilateral recognition agreements, we support a clear administrative due process prior to any preemption action to ensure that neither of these undesirable outcomes results from such action.

Second, we think it is important to explicitly direct that a portion of the funds appropriated to the FIO be used to secure and retain personnel with an appropriate level of insurance industry experience and expertise. As noted earlier, there is a significant gap in insurance industry knowledge at the federal level today. In order for the FIO to successfully fulfill its charge, it will be absolutely necessary to staff it from day one with personnel who are well versed in the workings of the industry. This becomes even more important given the need to have the FIO act as the federal expert on all things insurance in interactions with any future systemic risk regulator and international solvency matters. Additionally, Congress may want to consider establishing an insurance industry advisory committee that the FIO can look to and work with on important industry issues during the early years of its tenure to ensure it receives input from industry experts.

Third, we think it is important to clarify that the FIO is not to have any general supervisory or regulatory authority over insurance companies. We understand that that is the intent of the proposal, but as currently drafted there is ambiguous language that could cause confusion on this issue at some point in the future. The industry does not support adding an additional regulator on top of the 50+ we already have, and so we believe complete clarity of this intent should be stated within any final bill before it moves forward.

There are a number of additional general adjustments to the proposal that we recommend occur prior to its final enactment. Briefly, these include:

- Clarification that the FIO may represent the U.S. before any and all international organizations, as appropriate;
- Clarification that any information collected by the FIO directly from an insurer will be afforded the same confidentiality protection as information obtained by the FIO from a state or federal regulatory agency; and
- Expansion of the content contained in the FIO's annual report to Congress to include information on the state of the U.S. insurance regulatory system and updates on the FIO's ability to carryout its designated functions under the Act.

Mr. Chairman, we believe the need for establishment of the FIO is now self-evident and, with the addition of the changes we have outlined for you here today, we fully support enactment of the proposed substitute amendment to H.R. 2609. Thank you for giving us the opportunity to present our views, and we look forward to working with you and other members of this Committee as this legislation moves forward.