December 16, 2011

Mr. Michael T. McRaith
Director, Federal Insurance Office
Department of the Treasury
Federal Insurance Office, MT 1001
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Re: Public Input on the Report to Congress on How to Modernize and Improve the System of Insurance Regulation in the United States

Dear Mr. McRaith:

The Committee on Capital Markets Regulation (Committee) appreciates the opportunity to comment on the Federal Insurance Office's (FIO) notice and request for comment on the Report to Congress on How to Modernize and Improve the System of Insurance Regulation in the United States.[1]

Since 2005, the Committee, composed of 32 members, has been dedicated to improving the regulation of U.S. capital markets. Our research has provided an independent and empirical foundation for public policy. In May 2009, the Committee released a comprehensive report entitled *The Global Financial Crisis: A Plan for Regulatory Reform*, which contains fifty-seven recommendations for making the U.S. financial regulatory structure more integrated, more effective, and more protective of investors in the wake of the financial crisis of 2008.[2] Since then, the Committee has continued to make recommendations for regulatory reform of major areas of the U.S. financial system.

We believe that any attempt to modernize and improve insurance regulation should be based on an optional federal charter system with federal preemption. This position is consistent with past positions of the Committee in support of a streamlining and simplification of our overall regulatory structure.[3] The idea of a federal charter has gained traction in recent years, including for example in the proposed National Insurance Act of 2006[4] that was re-introduced in Congress several times since. We believe such a federal charter system would offer numerous benefits in efficiency and cost by streamlining existing regulation and replacing it with a uniform regulatory framework. It would also encourage competition at a single, national level, encourage

[1] Public Input on the Report to Congress on How to Modernize and Improve the System of Insurance Regulation in the United States, 76 Fed. Reg. 64,174 (proposed Oct. 17, 2011) [hereinafter Request for Comment].
[2] COMM. ON CAPITAL MKTS. REG., THE GLOBAL FINANCIAL CRISIS: A PLAN FOR REGULATORY REFORM (May 2009), http://www.capmktsreg.org/research.html [hereinafter the May 2009 Report].
[3] See COMM. ON CAPITAL MKTS. REG,, RECOMMENDATIONS FOR REORGANIZING THE U.S. FINANCIAL REGULATORY STRUCTURE (Jan, 14, 2009) ), http://www.capmktsreg.org/research.html; and the May 2009 Report.
[4] S. 2509, 109th Cong. § 2 (2006).

new entries in the insurance market, and reduce the speed to market for new products under the uniform standards of a single regulator.[5] As the FIO conducts its study, it should do so from the perspective of an optional federal charter as the ultimate goal.

A federal charter would reduce costs by reducing the number of licensing and compliance regimes insurers face, and allowing insurers to achieve economies of scale. Federal preemption is a critical element of any such proposal. While a single federal system poses immense potential benefits, a two-tiered system, where both federal and 51 separate state rules may apply, would increase regulatory complexity and would be a significantly worse outcome than the current system. A single consolidated regulator would also be able to deal more efficiently with other financial regulators, including regulators of banks and security firms, both in the U.S. and abroad, and "would give [U.S. insurers] a common regulatory regime more in line with their [international] competitors…."[6]

Opponents of an optional federal charter often cite inherent differences in insurance products attributable to geographic or cultural differences across states (for example, how to price property insurance in a flood-prone state, or insurance for theft in a state with high crime). To the extent that the FIO determines a federal insurance system should continue to address such differences through regulation, the FIO should consider whether a structure like that of the Federal Reserve, with a central Board of Governors and regional Federal Reserve Districts, might effectively address these concerns. We caution against a regime where the central federal regulator fully delegates certain of its responsibilities to the states, however, as such an arrangement could create uncertainty around ultimate federal preemption.

Other opponents of a federal charter have objected to federal preemption with respect to consumer protection-related issues. They argue that state regulators may be more responsive to local complaints because there are political consequences if they are not responsive.[7] There is a need for strong consumer protection to address issues including deceptive advertising, unfair policy terms, and discriminatory or unfair treatment of policyholders.[8] However, the new federal insurance regulator would be in the best position to assume these consumer protection responsibilities. As the single regulator promulgating and interpreting rules for the insurance industry, it would be well-positioned to address issues about how insurance products are sold and potential unfairness to policyholders. Furthermore, insurers would face a single set of consumer protection rules, resulting in efficiencies and cost savings.

We believe the federal consumer protection role should be given to the new federal insurance regulator rather than to the Bureau of Consumer Protection (CFPB). Unlike the case in

[5] Michael Bloomberg and Charles Schumer, "Sustaining New York's and the US' Global Financial Services Leadership" 117 (Jan. 2007), www.*nyc.gov/html/om/pdf/ny_report_final.pdf* [hereinafter the Bloomberg-Schumer Report.].
[6] Bloomberg Schumer Report at 117.
[7] Hal S. Scott, Prepared Written Testimony before the Committee on Banking, Housing and Urban Affairs, U.S. Senate 7 (July 28, 2009), http://www.capmktsreg.org/testimony.html [hereinafter Written Testimony].
[8] HENRY M. PAULSON ET AL., THE DEPARTMENT OF THE TREASURY, BLUEPRINT FOR A MODERNIZED FINANCIAL REGULATORY STRUCTURE 131 (Mar. 2008), http://www.treasury.gov/press-center/press-releases/Pages/20083311051120043.aspx.

banking regulation, where consumer protection played a secondary role to safety and soundness concerns, consumer protection is the major focus of insurance regulation. The concern with safety and soundness in insurance regulation is not principally to protect against systemic risk but rather to make sure insurance companies can honor their obligations to policyholders.

In determining the ideal structure for a federal insurance regulator, the FIO should consider existing state insurance regimes to determine what has worked well at the state level, and also what features have needed improvement. We also note that certain features of a state insurance system may not be appropriate at the federal level and vice versa. For example, multimember insurance commissions are absent among the states, which suggests a structure like that of the Federal Reserve may not work at the federal level. However, they may be more necessary at the federal level to achieve political balance.[9]

Thank you for considering our comments. Please do not hesitate to contact us at (617) 384-5364 if we can be of any further assistance.

Respectfully submitted,

Robert Glenn Hubbard
R. Glenn Hubbard
CO-CHAIR

John L. Thornton
CO-CHAIR

Hal S. Scott
DIRECTOR

[9] Hal Scott, "Optional Federal Chartering of Insurance: Design of a Regulatory Structure," Harvard Law School Public Law Research, Paper No. 07-05 (March, 2007), pp. 13-14.