



NCOILETTER

December 2006

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NATIONAL CONFERENCE OF INSURANCE LEGISLATORS

Preserving State Insurance Regulation...

- By interacting with Congress on issues of critical importance to insurance public policy
- By educating state lawmakers on the solutions to their insurance-market crises
- By fostering relationships between state legislators
- By asserting the primacy of state insurance regulation under the McCarran-Ferguson Act of 1945

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NAIC MOVES REINSURANCE COLLATERAL PROPOSAL, SETS COURSE FOR REGULATORY SEA CHANGE

Regulators gathered at the National Association of Insurance Commissioners (NAIC) Winter Meeting in San Antonio early this month moved one step closer to adopting an entirely new system for evaluating foreign and domestic reinsurance collateral requirements.

On December 9, the Reinsurance Collateral Task Force endorsed a resolution calling for creation of a Reinsurance Evaluation Office (REO) within the NAIC that would evaluate the operating integrity and financial strength of reinsurers, without regard to jurisdiction, based on data from national rating organizations and other sources.

Under the plan, the REO would place each reinsurer in one of six categories. Each category would correspond to a percentage of minimum collateral a reinsurer would be required to post. For instance, companies rated REO-1 would be free of collateral requirements, while those in REO-6 would post 100 percent.

Initially, the Task Force plan had even the strongest reinsurers posting 20 percent collateral and called for creation of only five rating categories. However, in response to strong U.S. industry con-

cerns that such stiff collateral mandates would unravel the benefits of U.S. licensure, regulators recently revised the plan to eliminate all collateral requirements for domestic reinsurers in any one of the top three categories—REO-1 through REO-3.

Outgoing NAIC President and ME Insurance Superintendent Al Iuppa earlier this year committed the NAIC to taking decisive action on the collateral issue by the end of 2006, noting that regulators had deliberated for many years. FL Insurance Commissioner Kevin McCarty, who sits on the NAIC Task Force, said after the vote, "The message is being sent out loud and clear that this is a paradigm shift in terms of how we view alien [non-U.S.] reinsurers." Under the current regulatory scheme, non-U.S. reinsurers must post 100 collateral for ceding companies to take credit for their foreign reinsurance.

David Matcham of the International Underwriting Association applauded the Task Force action, saying, among other things, "Any collateral requirement needs to be based on principles of financial strength rather than geographic location."

However, domestic reinsurers were clearly unimpressed.

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NCOIL IN ACTION

At the NCOIL Annual Meeting, legislators took the following public policy actions, among others:

- Adopted a proposed **market conduct** model law, as well as a resolution supporting expanded **annuity suitability** standards
- Readopted NCOIL **identity theft** and **company licensing** model acts
- Postponed indefinitely proposed **long-term care partnership** models
- Moved for further consideration a proposed NAIC **mega-catastrophe** plan, and voted to convey initial comments to regulators
- Moved for further consideration proposed models regarding **PEOs, PBMs, physician discount** secondary markets, uniform **building codes, reinsurance collateral**, as well as development of a **payday lending** model and review of an NCOIL **life settlements** model

VIEW FROM THE HILL: THE NEW CONGRESS

By Kevin Horan

With election results in and Democrats ready to take control of both chambers, many observers are asking, what does this mean for the insurance industry?

Over the last 12 years, Republicans have worked on efforts including an overhaul of the tort liability system, reform of class-action litigation, changes in bankruptcy law to make it harder for borrowers to escape paying debts, and limits on shareholder lawsuits, among other things. They also have proposed legislation regarding small employer access to health insurance. NCOIL opposes this well-intentioned initiative.

With Democrats now in power, these efforts will lose traction. Democrats and their allies will be looking for a certain degree of payback. The trial lawyer lobby, for instance, wants to replace the Republicans' tort reform campaign with a focus on such things as opposing mandatory arbitration clauses that restrict consumers' ability to sue entities like creditors, insurance companies, and loan providers.

Expect to see alternatives to the Republicans' healthcare proposals, including what are primarily Democratic attempts to close the Medicare Part D "doughnut hole" and what is perhaps growing interest in a more "universal" approach to covering the uninsured.

Troublingly, consumer groups and trial lawyers are among those asking Congress to explore removing the limited antitrust exemption for the insurance industry, which was established under the 1945 McCarran-Ferguson Act and which NCOIL adamantly supports.

Incoming Senate Judiciary Committee Chairman Patrick Leahy (D-VT)

has previously sponsored legislation that would repeal the exemption for medical malpractice insurance. He also is a co-sponsor of outgoing Committee Chairman Arlen Specter's (R-PA) bill to repeal the McCarran antitrust exemption across the board. Leahy has charged that, under the exemption, insurers have the ability to collude on rate-setting and therefore prevent free-market competition.

Incoming Senate Banking Committee Chair Chris Dodd (D-CT) is a mystery to many, having spoken little on insurance issues. That said, there is one item we know for sure that he will run with—continuing the federal government's terrorism risk insurance program, which expires at the end of 2007. Dodd's staff has told NCOIL that this will be one of the first issues the Banking Committee deals with. In the past, Dodd has advocated for making the federal backstop permanent despite opposition from the White House, which favors a free-market approach.

In the House of Representatives, word on the street is that incoming Financial Services Committee Chairman Barney Frank (D-MA) will allow Rep. Paul Kanjorski (D-PA) to take the lead on insurance matters when he assumes chairmanship of the Capital Markets, Insurance, and Government-Sponsored Entities Subcommittee. In the past, Kanjorski has expressed some support for an optional federal charter, something that Frank has opposed.

With a new Congress and new leadership in place, it is hard to say what issues will emerge as insurance priorities next year. We know for sure that terrorism risk insurance will be at the top of the agenda. NCOIL over the coming months will be meeting with the new chairs and other members of the committees and their staff to communicate our positions and to forge new working relationships.

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NCOIL ADOPTS MARKET CONDUCT MODEL, CLOSES DEBATE

Lawmakers at the recent NCOIL Annual Meeting in Napa Valley, California, reasserted the need for a modernized market conduct surveillance system by adopting an NCOIL model act that would establish uniformity of market conduct oversight. The *Market Conduct Surveillance Model Law*, adopted by the NCOIL Executive Committee on November 11, would end costly duplications regarding market conduct exams and follows more than five years of NCOIL work on the issue.

Rep. Craig Eiland (TX), chair of the NCOIL State-Federal Relations Committee that initially examined the model, stated, "This action was a long time in coming. NCOIL's goal with the model law—which we expect will garner strong support in the states—is to cut down on duplications in state market conduct exams while still giving regulators the ability to do their jobs and protect consumers."

Rep. Eiland continued that "The model offers common sense guidance on how to monitor insurer actions in a coordinated, efficient, and effective

way. It is now critical that legislators bring this model to their states and follow the leads of Texas and Colorado in enacting needed statutory reform."

The model would, in part, 1) establish methods for collecting marketplace data; 2) allow domiciliary states to have responsibility to perform market conduct surveillance; 3) enhance state collaboration; 4) set forth a continuum of market conduct actions to be considered prior to undertaking targeted market conduct exams; and 5) set forth a structure for performing those examinations.

Passage of the NCOIL model followed consideration of recommendations, offered by a Market Conduct Subcommittee, to amend a February 2004 NCOIL draft in place of a joint NCOIL-NAIC model, adopted later in 2004, that had received little regulatory and industry support in the states.

The Subcommittee revisions reflected input from a range of interested parties both before and immediately following the 2006 NCOIL Summer Meeting.

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ILF RELEASES RFP REGARDING STUDY ON STATE INSURANCE AUTHORITY

The Insurance Legislators Foundation (ILF) of NCOIL has released a request for proposal (RFP) regarding *A Study on State Authority: Making a Case for Proper Insurance Oversight*.

The RFP notes that recent events have blurred the lines of responsibility regarding state insurance regulation. These include investigations into broker disclosure and finite reinsurance; the introduction of federal preemptive initiatives, including optional federal charter and federal tools efforts; the movement toward financial modernization; and the ever-increasing globalization of insurance.

The objective of the study would be to explore the legal authority behind primary oversight of insurance and related consumer protections;

distinguish between the statutory authorities/responsibilities granted to legislative, executive, regulatory, and judicial branch members, among others; and offer case studies regarding the evolution and funding of regulatory entities.

The report also would provide recommendations to clarify and define the role of such entities and their oversight duties in order to promote an effective, efficient regulatory environment.

The scope of the *Study* would include 1) the nature and history of insurance regulation; 2) laws/rules/procedures identifying jurisdictional responsibilities of officials in governing insurance policy and related consumer protections, including issues as to the authority that may

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SAVE THE DATE

NCOIL Spring Meeting & Seminar

March 1 through 4, 2007

Savannah, Georgia

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NAIC MOVES REINSURANCE COLLATERAL

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U.S. companies assert that the current system protects consumers and that any reduction in foreign collateral requirements would pose a serious threat to the U.S. insurance industry. Frank Nutter of the Reinsurance Association of America said after the Task Force vote, "We think the current system has worked well to foster capacity. The REO proposal is flawed."

Opponents of the REO plan contend that it is vague on critical issues, including the NAIC's ability to evaluate the financial strength of foreign reinsurers, and that regulators did not give due consideration to certain interested-party alternatives. Mike Koziol of Property Casualty Insurance Asso-

ciation of America commented that an industry idea to establish some sort of working trust mechanism, in which carriers could draw down funds as claims are paid, would be a "more vibrant scheme."

The Reinsurance Task Force resolution, in addition to supporting creation of the new REO system, calls on the NAIC Financial Condition Committee to flesh out the proposal next year in response to U.S. reinsurer concerns. A full NAIC vote is contemplated for September 2007.

NCOIL has long examined the collateral issue and urged the NAIC to take decisive action. Legislators began considering the REO plan at the NCOIL Annual Meeting and will more fully explore the draft at the group's 2007 Spring Meeting.

CONGRESS ACTS ON SCHIP REAUTHORIZATION

In the waning hours of the 109th Congress, lawmakers passed a stop-gap measure to address perceived immediate funding shortfalls in the State Children's Health Insurance Program (SCHIP), redistributing \$275 million from states with unused funds to those facing shortfalls.

Although the stop-gap measure will provide extra money for 14 states at risk of running out of financing, the program will run out of funds in May.

SCHIP, which enrolls more than 4 million low-income children who may otherwise be uninsured, was created in 1997 and authorized for fiscal years 1998 through 2007 as a federal block grant with a fixed annual funding level that does not increase with rising health care costs. As a result, Con-

gressional Research Services estimated that 17 states lacked sufficient funds to maintain their SCHIP services. Without a more permanent increase in funding levels, the Centers for Medicare & Medicaid Services estimated that in 2012 only 2.9 million children will remain enrolled.

In the late 1990s when SCHIP was in its infancy, funding was less of an issue because states that overspent their SCHIP allotment were allowed to draw upon unspent funds from other states. However, as more states began developing programs, and the cost of program delivery increased with rising health care costs, the amount of unspent funds shrunk dramatically.

The NCOIL Health Insurance Committee will discuss SCHIP during the March NCOIL Spring Meeting.

ILF RELEASES RFP

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be due non-profit corporations and similar entities; 3) case studies explaining the evolution of the current insurance regulatory environment, including growth of assets and data utilization/security; and 4) the extent and effectiveness of intra-governmental communication/cooperation.

The study also would examine the impact that functional regulation, as established by GLBA, has had on insurance oversight and responsibility, and

the impacts of federal preemptive efforts on insurance policymaking.

The role NCOIL and other state legislative groups, the National Association of Insurance Commissioners, National Governors Association, National Association of Attorneys General, and others play in insurance public policy will be included.

The ILF is NCOIL's educational and research arm. The RFP is available at www.ncoil.org. Proposals are due by January 5, 2007, at 5 p.m. (EST).