Comments by the National Association of Professional Insurance Agents in response to the Notice and request for comment regarding:

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

Department of the Treasury, Federal Insurance Office

Introduction

The National Association of Professional Insurance Agents (PIA) is a national trade association founded in 1931 which represents member insurance agents in all 50 states, Puerto Rico and Guam and their employees who sell and service all kinds of insurance, but specialize in coverage of automobiles, homes and businesses.

PIA agencies provide their individual clients with personal lines and commercial lines insurance. In addition, many PIA agencies offer life and health insurance products. These agents are active business leaders in their communities and are in the unique position of working closely with both insurance companies and consumers.

We appreciate this opportunity to offer our comments as the Federal Insurance Office (FIO) conducts its congressionally-mandated study on modernization of the insurance regulatory system in the United States.

PIA National believes that the fundamental public purpose and obligation of all regulation is the safety and protection of the people. This includes supporting a sound and competitive marketplace, but it also requires oversight of commercial participants together with enforcement of applicable laws for the benefit of the public.

It is apparent from the questions specified in FIO’s enabling statute and in the subsequent request for comment published in the Congressional Record that an assessment of potential federal regulation of insurance is a part of this study.

In our comments, we propose four principal recommendations:

1. That we believe insurance is efficiently regulated by the states and independent agents play a valuable role in serving consumers.

2. That FIO should support and compliment state regulation of insurance without federal preemption of state laws.

3. That FIO could help in addressing some of the licensing challenges faced by producers by:
   a. supporting the National Insurance Producer Registry (NIPR);
b. Helping to resolve foreign corporation issues;
c. Helping to resolve current conflicts among states in implementing NRRA.

4. That FIO should work to ensure the solvency, soundness and availability of financial response on the part of foreign carriers operating in the U.S. domestic market.

We must note at the outset that PIA is strongly opposed to expanded federal regulation of insurance and is in equal measure strongly supportive of a modernized, national state based system of insurance regulation. That said, we can be supportive of the FIO as long as it adheres to the mandate set for it by Congress that specifies it is not a regulator of the business of insurance, a role that the FIO correctly notes has been reserved for the states. We also believe that any recommendation FIO makes to Congress as a result of this study, or more generally, to alter this restriction would be ill-advised.

PIA believes that a modernized insurance regulatory system must remain state based and that insurance consumers, the insurance industry and the American economy would be poorly served by expanding federal insurance regulation, either in whole or in part.

Contrary to some assertions, the state based system of insurance regulation is not broken. It has performed exceptionally well, especially during the 2008 financial crisis. The Gramm-Leach-Bliley Act of 1999 specified that our financial system is, for purposes of regulatory oversight, divided into three sectors: banking, securities and insurance; it additionally specified that the insurance sector was to continue to be functionally regulated by the states while the banking and securities sectors would fall primarily under federal supervision.

During the economic collapse of 2008, the insurance industry and the policyholders it serves were protected, largely due to prudent supervision by state insurance regulators that ensured financial stability, safety and soundness. At the same time, failed federal regulation in the banking and securities sectors contributed greatly to the collapse.

Rather than embrace the recommendations of former Treasury Secretary Henry M. Paulsen in his 2008 *Blueprint for a Modernized Financial Regulatory Structure* that insurance regulation be absorbed into the federal regulatory structure that failed, we should seek to build upon the success of our national state-based system of insurance regulation in protecting policyholders, the insurance industry and America’s economy. This is the blueprint we propose.

In fact, there are lessons to be learned by banking and securities regulators in the successes of the national system of state based insurance regulation, which could be the subject of other reports.

There is an assumption underlying the questions posed in the statutory mandate to the FIO to conduct a study of insurance regulation and report to Congress with recommendations. The questions were weighted with an assumption that modernization equals federalization. For example, one question specifies assessing “the costs and benefits of potential federal regulation of insurance across various lines of insurance
except for health insurance.” There is no provision for also assessing, or even acknowledging, the disadvantages of potential federal regulation of insurance across various lines. One purpose of our comments here is to specifically challenge this underlying assumption and address key omissions.

Modernization of insurance regulation does not mean federalized regulation, any more than protection of insurance consumers requires federal preemption of state consumer protection authority. The national state based system of insurance regulation is more modern, more efficient and more effective than any potential federal construct in insurance, or existing federal constructs in the banking and securities sectors.

We believe, however, the FIO can play an immediate, constructive role in helping the states significantly improve the existing insurance regulatory system by working cooperatively with state regulators and legislators.

**Modernization without preemption**

Modernization of insurance regulation can work without preemption, as long as there is an effective, efficient regulatory system that continues to protect consumers and foster fair competition. Each jurisdiction is going to have to trust one another to regulate effectively, although checks and balances should remain.

For example, California recently announced it would no longer require non resident producers to submit fingerprints for background checks if they have already done so in their resident state. Prior to this decision, a producer would have to submit fingerprints to California even if they had already done so in their resident jurisdiction. This placed a huge burden on the state with very little consumer protection enhancement. Every so often, a producer that passed their resident jurisdiction background check would be rejected by California, but the consumer protection this afforded was not worth the tremendous time and effort the department had to expend, so they agreed to the change. Similarly, most states have made adjustments to become more uniform and reciprocal because they see consumer protections are not weakened and the system becomes more efficient for industry and regulators.

Flows of capital can be global because money is fungible. Insurance, by contrast, is geographically specific. All property-casualty personal lines and most commercial lines insure assets that exist in a fixed, physical place. State insurance regulators are best equipped to supervise the business of insurance because they have the local expertise needed to regulate what is essentially a local, not a global, financial service.

Federal preemption would inhibit modernization efforts by restricting the states’ ability to serve their markets. Generally, mechanisms to ensure consumer protection are more effective and efficient the closer they are to the consumers and communities being served.
We have seen how attempts at preemption can cause conflicts between state and federal regulators in the banking sector which can drag on for years; these conflicts have often been detrimental to consumers. For example, the Office of the Comptroller of the Currency (OCC) has in the past been aggressive in preempting state insurance consumer protection statutes, on the questionable rationale that they were in conflict with the National Bank Act of 1865. These actions were taken administratively by one federal agency, which relied solely upon its own interpretation of the law. Such federal preemption action constitutes regulatory overreach which invites federal-state conflicts, causes regulatory confusion, prompts lawsuits to address jurisdictional disputes and ultimately hurts consumers.

We are concerned that a similar use of preemption or threats of preemption in an effort to bring about regulatory modernization in the insurance sector would be similarly counter-productive. There may be a temptation at the federal level to use preemption to short-cut the necessary process of building consensus for reforms to modernize the national system of state based insurance regulation, however this approach is rife with the potential for unintended consequences. In contrast, a more effective way to bring about desired results is for the FIO to serve as a leader and a catalyst to effect changes.

The FIO has a platform to advise states on how they should operate, but because it is not a regulator, it should not be in the position of telling states how they must operate. By working with state regulators and legislators, both individually and through organizations like the National Association of Insurance Commissioners (NAIC) and the National Conference of Insurance Legislators (NCOIL), FIO can lead by promoting model laws and proposing certain changes to modernize the system.

**Producer licensing – specific fixes**

The future of producer licensing is a modernized, nationwide state-based electronic system, similar to the state securities regulators’ CRD, the Central Registration Depository licensing system. Just like the securities licensing system, the insurance producer licensing system was built and funded by the states and should remain under state control. The National Insurance Producer Registry (NIPR) has brought us from the old paper system to the modern age of electronic licensing.

NIPR works very well for the states that fully utilize it. Today, a producer can obtain a non-resident license electronically through NIPR in almost every jurisdiction. Most states, including Illinois, are on board with the uniformity efforts but some jurisdictions have historically been less cooperative. The process is not completely seamless nationwide because several jurisdictions – while participating in NIPR – retain some rules that are incompatible because they require some processes to be done in a unique way. This is not due primarily to any inherent resistance by the states; rather, it is the result of what can be best described as a few “glitches” in the system that need to be worked out, much as any new system has glitches.
In many instances, remaining barriers are unintentional and stem from longstanding legacy practices that have been retained for no compelling reason, offering little or no real consumer protection enhancement.

We believe that it is possible to get outlier states more fully onboard and that significant progress could be made in 2012. Perhaps certain regulatory standards, like licensing, could be a part of a regulatory accreditation process based on the successful financial accreditation standards program.

If every jurisdiction would adopt the Producer Licensing Model Act (PLMA), follow the recommendations in the NAIC producer licensing handbook and fully utilize NIPR, we would have the licensing system largely complete. This is an achievable medium-term goal. The FIO could accelerate this process by encouraging all states to adopt the PLMA.

**Foreign corporation and business entity licensing**

The foreign corporation issue can present a significant impediment to licensing modernization, if not done correctly. We appreciate the work the NAIC has done in this area in terms of education and recommendations that producer licenses should not be held up by duplicative demands from the secretaries of state.

The foreign corporation issue is tied to the licensing of business entities. Some have proposed the complete elimination of licensing of business entities. A few jurisdictions do not license entities but the majority of regulators, and some in the industry, support the option of requiring a business entity license. When a business entity becomes licensed on a non resident basis, the secretary of state will sometimes intercede and impose further licensing barriers that violate the Gramm-Leach-Bliley Act (GLBA).

The FIO can be helpful in pointing out instances where GLBA is not being followed, then recommend and assist states with compliance. PIA recommends that states not force business entities to obtain a non resident business entity license, particularly if the business entity is licensed in their resident jurisdiction.

State compacts are becoming an increasingly attractive option to achieve modernization. The PLMA, along with the successful Interstate Insurance Product and Regulation Commission (IIPRC) and now surplus lines reform, provide a framework for states to work cooperatively toward modernizing the state based insurance regulatory system.

**Crop Insurance – Overview of a Unique Product**

Crop insurance is a specialized product that provides financial protection to America’s farmers and is this country’s greatest agricultural safety net. It has a unique regulatory relationship to the federal government and is authorized by the Federal Crop Insurance Act to promote agricultural and economic stability.
The federal crop insurance program is administered by the Federal Crop Insurance Corporation (FCIC), a government corporation within the United States Department of Agriculture (USDA). The FCIC’s activities are administered by the USDA’s Risk Management Agency (RMA). The FCIC regulates the business of crop insurance and oversees the rates, terms, and conditions of federal crop insurance contracts.

While crop insurance was initially sold directly by the federal government, a public/private partnership developed beginning in 1980 to better serve the agricultural community. Previously, direct federal sales of crop insurance was found to be unsuccessful, with the costs to the USDA of administration increasing while the take-up rates by farmers was decreasing.

Since the institution of a public/private partnership for the delivery of crop insurance, administrative costs have gone down, take-up rates have increased appreciably and the program has been a net positive contributor to the federal budget in most years. Professional independent crop insurance agents are now the main source for crop insurance sales and their dedication to their role has become evident through the incredible growth the program has seen since their increased involvement. The program continues its successful operation under the 2008 Farm Bill.

Administrative imposition of federal price controls in crop insurance

However, the 2008 Farm Bill authorized the renegotiation in 2010 of the Standard Reinsurance Agreement (SRA), the contract governing financial and other terms between the federal government and private sector insurance companies. Insurance agents do not have a formal voice during these negotiations. A new SRA was negotiated and signed last year. The new SRA was significant in that it represents the first time that the federal government has attempted to impose price controls on the free market participants in the public/private crop insurance program.

First, the 2010 SRA radically changed the reimbursement rate for certain government paid administrative and operating (A&O) expenses. This led to major cuts to many states that were expecting higher payments, including many states that USDA maintained the SRA was intended to benefit.

Secondly, the SRA imposed caps on the compensation a private company may pay private agents for the delivery of insurance. The change in the way in which crop insurance agents are compensated is a wholesale departure from time-honored industry practice with respect to the delivery of property and casualty insurance, which has always been, and by and large remains, expressed as a percentage of total premium.

This led the federal government to become involved in the wholly private contracts between wholly private companies and private agents to cap agent compensation. As such, the cap is arbitrarily set by the government and bears no relationship whatever to factors reflected when the private market sets the same terms. It is analogous to federally mandated price controls.
Because of this, PIA crop insurance agents in multiple states are reporting compensation cuts of up to 55% of their pay. Insurance agents pay a critical role in the success of the Federal Crop Insurance program. They are the face of the program, selling and serving policies to farmers throughout America’s rural communities, assuming significant administrative duties which they pay for from their total compensation, relieving the federal government and crop insurance companies of those expenses, while taking a federally-mandated pay cut.

We do not believe that it is a proper role for the federal government to take administrative action that dictates the maximum compensation of a private insurance agent, for any line of insurance. The decision to do so has negatively impacted a vital part of the crop insurance delivery system. While PIA continues efforts to repeal these compensation caps, we would be similarly opposed to comparable action on other lines of insurance.

PIA cautions Congress against granting any federal entity the kind of statutory authority which could be broadly interpreted administratively to permit the de-facto imposition of federal price controls on private sector participants in public/private partnerships with the federal government. Adopting omnibus legislative language specifically prohibiting such action by federal agencies is highly advisable.

**Nonadmitted and Reinsurance Reform Act**

The Nonadmitted and Reinsurance Reform Act (NRRA) is a federal law with requires commonality among state authorities. There are three main parts to implementing NRRA in the U.S. marketplace:

1. A common, modern, streamlined, simplified, clear E&S taxing method embraced by all states.
2. A simplified, streamlined reporting process used and fully embraced by all states.
3. A modern and streamlined E&S resident and nonresident licensing process that:
   a. Does not subject qualified E&S resident brokers to a dual-license system which requires them to secure a nonresident producer license before they can secure their nonresident E&S broker license in each nonresident state;
   b. Is the E&S licensing system common among all states;
   c. Continues to make clear (which aligns with insurance law) that E&S brokers are responsible for having and exercising the E&S compliance expertise in all states in which they conduct business;
   d. And that nonresident E&S brokers may not transfer/place the burden of E&S compliance and/or tax process onto the shoulders of the resident retail insurance producer (who in a majority of cases generates the E&S business to be placed with nonresident E&S brokers).

Proper resolution among the states is not solely in the hands or under the authority of the NAIC or state insurance commissioners to resolve. This will require FIO to add to the
working group of NAIC and state insurance commissioners, state legislators, the National Governors Association and state comptrollers, all of whom have a state authority role in this, and in many states are or can be the driving or primary state authority controlling end results. This is another example of why PIA National has always favored all-state compacts for insurance, so that there is a legal framework to encourage commonality with regard to both intrastate and interstate issues. All-state compacts also provide a framework to address state-federal domestic issues and can facilitate cooperative efforts to address international issues.

Outreach to historically underserved communities

Everyone can benefit from having insurance. Unfortunately, some consumers can face obstacles in obtaining the insurance coverages which would benefit them. In order to expand opportunities to those who have been historically underserved, we need to examine some of the reasons for this situation.

Insurance illiteracy: Even the most financially sophisticated consumers can have a deficit of understanding about insurance. While U.S. school systems have many formal programs teaching rudimentary financial survival skills, such as how to balance a checkbook or draw up a household budget, budget pressures have greatly reduced and restricted these programs as a part of the formal school curriculum. PIA members are advocates for and engage in public/private partnerships that bring this education back to the schools. In doing so, PIA aims to see that teaching about insurance is part of the package. It is never too early to begin teaching students about the financial services industry, its segments, how to access and use it and how it serves their interests. In this regard, we should consider all students underserved since the vast majority simply lack a basic understanding about finance and insurance, because it is not traditionally a topic taught by and within families.

Cultural barriers: In some foreign cultures, insurance does not exist. Immigrants from these cultures have formed no concept whatsoever about insurance, creating a heightened need for education to overcome this barrier.

Research conducted in the 1990’s by the National Association of Professional Insurance Agents concluded that insurance carriers generally were interested in outreach to underserved communities. Further, our published results in Doing Business With the New Insurance Consumer (1996) found that people in many traditionally underserved communities relied greatly on personal recommendation when making decisions about insurance. Our study found that in many culturally diverse communities, the personal contact, education and service provided by professional independent insurance agents could overcome resistance to the utilization of insurance products. This outreach must be community-based to succeed, and professional independent insurance agents have always fulfilled the role of community-based educators about insurance.

PIA believes that a successful outreach to historically underserved consumers is critical to the growth of a sound financial future for consumers and the U.S. economy. In support
of this belief, PIA is willing to expand its current activities to work with the FIO to develop innovative programs to better reach minority communities and expand the number of independent insurance agents and agencies in these communities. As part of this commitment, PIA wishes to make clear that every minority-community independent insurance agent in the nation is invited to become a member of our association. There have never been any barriers in our organization.

Having more than one professional independent insurance agency in every underserved community in the United States would be an effective step toward a fully inclusive insurance industry. But, in order to serve the traditionally underserved, PIA inner-city insurance agencies also need innovative insuring programs offered by insurers willing to empower change and progress.

**Conclusion**

The statutory restrictions Congress placed on the FIO make clear that the FIO was never envisioned as a regulator of the business of insurance in the United States, either wholly or partially. In our view, this is the correct approach, and the FIO should never seek to expand its mandate, either administratively or by advocating subsequent legislation to that effect.

Instead, the FIO should assume a complimentary role to the existing national system of state-based insurance regulation. The FIO should not assume a competitive stance relative to state insurance regulatory authorities. In addition, we believe it is imperative that the FIO cultivate a cooperative relationship with state insurance legislators, who determine domestic insurance regulatory policy which is then carried out by state insurance regulators.

PIA believes the FIO can play a positive role in helping states meet their uniformity and reciprocity goals. The FIO can promote adherence to model laws and regulations and help states make positive changes in their current practices. Because one size does not fit all, we will have to balance our desire for uniformity and reciprocity with the need for states to retain the flexibility necessary to best serve their markets.

**Appendix:**

*PIA’s Roadmap to State Regulatory Modernization* (published 2008)

Foreign Corporation Filings (PIA statement submitted to NAIC, 6/11/07)