

**U.S. House of Representatives  
Committee on Financial Services  
Subcommittee on Capital Markets, Insurance, and Government Sponsored  
Enterprises  
Hearing on "Working with State Regulators to Increase Insurance Choices for  
Consumers"  
March 31, 2004**

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Mr. Chairman, Members of the Subcommittee, my name is Roger Singer and I am Managing Director, Senior Vice President and General Counsel of OneBeacon Insurance Group, a multi-line organization of affiliated property and casualty insurance companies headquartered in Boston, Massachusetts, and operating through a network of regional and branch offices. OneBeacon is licensed in all 50 states, and markets its insurance products through independent insurance agents and brokers, principally in the New England states, New York, and New Jersey. I want to thank the subcommittee for allowing me to present my views today on behalf of OneBeacon and our property and casualty insurance trade association, the American Insurance Association (AIA).

I have been general counsel to OneBeacon and its predecessors for the last fifteen years. Prior to joining OneBeacon, I served as commissioner of insurance for the Commonwealth of Massachusetts from 1987 to 1989. Prior to my being insurance commissioner, I served in other capacities in Massachusetts state government as well as in the federal government at the Federal Trade Commission. I believe my background enables me to address the important issue before you today – national reform of the state insurance regulatory system – with my experience informed by being, at one time or another, on both sides of the insurance table: as an insurance regulator, and as an insurance company executive.

Because of OneBeacon's national scope and regional focus, we have familiarity with the full range of insurance regulatory systems employed and administered by the states and the District of Columbia. Fifty-one jurisdictions, operating independently of one another, have led to a patchwork-quilt regulatory system that creates inefficiency and is ultimately harmful to consumers. Even within each jurisdiction, there are often differing systems for different lines of business, making the process incredibly cumbersome and unresponsive to consumer needs. A limited survey by AIA of state requirements found approximately 350 that dictate how rates are to be filed and reviewed, and approximately 200 that relate to the filing and review of new products. National and regional companies often make thousands of filings each year. Last year, OneBeacon completed 454 filings in its eight "core" states alone. Add up the months and even years that it takes to review a company rate or form filing, and one does not have to be an actuary to calculate the cumulative inefficiency the state regulatory process imposes on the marketplace.

The National Association of Insurance Commissioner's (NAIC) efforts, while well-intentioned, can only go so far to produce uniformity and consistency of regulation. The NAIC can draft and adopt models, but cannot force state legislatures to enact them. Similarly, individual state insurance regulators can push for regulatory modernization in their own respective jurisdictions, but they cannot force other state insurance regulators to push for similar change. The history of post-McCarran Ferguson Act state insurance regulation demonstrates that structural change requires a federal push.

Sensing the urgent need and momentum for change, this subcommittee has called for systemic reform of rate, policy form, company licensing, and market conduct regulation, with a coordinated state-federal oversight role in each of these areas. And make no mistake about it, systemic reform is precisely what must occur for the good of insurance consumers and the health of the insurance marketplace.

Like other member companies of AIA, OneBeacon supports a market-based optional federal charter as the best way to achieve needed reforms with the least disruption to the state system. But, like AIA, we must be pragmatic about the pace of reform in the short term. Done correctly with appropriate reliance on market forces, targeted reform will: a) lead to national uniformity; b) reduce regulatory red tape; and c) enhance consumer protection by shifting regulatory attention and resources away from government price and product controls and toward ensuring financial stability so that insurance companies are able to pay claims when they arise.

In the area of insurance rates, the subcommittee's stated goal is to eliminate government price controls and to instead rely on Illinois-style, free-market competition. This is a significant step toward placing insurance on a level regulatory playing field with other non-monopolistic industries. In many ways, property and casualty insurance is the last outpost of the discredited economic theory of government price regulation. Government price controls do not work to the benefit of anyone – especially consumers. In states where rigid government price controls are prevalent, insurance premiums are higher and rates more politicized, consumer choices are restricted, residual markets are larger, and the number of competing insurers is lower.

The Massachusetts automobile insurance market provides a stark example of the unintended consequences of price controls. In Massachusetts, automobile insurance rates are set by the insurance commissioner, unless the commissioner determines (at an annual hearing) that sufficient competition exists to assure that rates will not be excessive. State-made rates are the worst form of government price controls, even worse than a strict prior approval system. The commissioner considers a number of factors when making this competitiveness determination, including whether a finding of competition will result in immediate rate increases. Inevitably, because of the political risk that a competitive market finding might trigger price increases, such a finding has never been made and rates continue to be set by the commissioner. This was the case when the very first decision was made under the statute in the 1970's, was the case when I was Massachusetts insurance commissioner during the late 1980's, and remains the case today. Unfortunately, my public sector and private sector experience has confirmed that the political consequences of moving directly to market-based rate regulation – the fear of short-term price spikes – often dooms any movement in that direction altogether.

Yet, there is plenty of evidence that elimination of Massachusetts' price control system for automobile insurance not only would result in lower premiums, but a healthier marketplace. When compared with Illinois, the one jurisdiction without any government price controls, Massachusetts falls well short – whether the comparison is measured by average automobile insurance premiums, number of drivers in the subsidized residual market, or number of competitors. The two state comparisons are not even close. Based on the latest available data from 2001:

- average annual automobile insurance premiums in Illinois were \$748, compared with \$1,013 in Massachusetts;
- 273 auto insurers actively competed for business in Illinois, compared with 38 automobile insurers competing in Massachusetts.
- 7.5% of Massachusetts drivers were in the residual market, compared with 0.02% of Illinois drivers;

In fact, one could argue that the percentage of drivers in the Massachusetts residual market is functionally closer to 25% because of Massachusetts' "exclusive representative producer" system – a system whereby over 25% of automobile insurance premium is produced by insurance brokers involuntarily appointed to insurers. In addition, the number of Massachusetts automobile insurers continues to shrink, as the latest numbers show only 20 carriers currently writing such insurance.

The differences between Illinois and Massachusetts are not surprising. Price controls can have the politically expedient short-term effect of holding insurance rates down. However, if left in place, those controls act as an artificial pressure cooker that hurts competition, masks systemic costs, leads to higher prices, and forces consumers into residual markets.

With respect to regulation of insurance policy forms, rather than a market-based system, the subcommittee has proposed a single point-of-filing with expedited review based on clear standards. This is a useful point of departure for examining alternative reform proposals. In jurisdictions with strict product controls, the government review process for product filings can take months or years from filing to approval, with product denial attached to unpublished, arbitrary "desk drawer" rules or regulations that have only tenuous connections to underlying statutory standards.

This process is especially frustrating for companies trying to roll out products regionally or nationally. The system provides no incentives for insurance product innovation. In turn, consumers have fewer different marketplace choices and no real basis to compare insurers by the products they offer. This process inhibits innovation and frustrates consumer choice.

Three principles should underlie the subcommittee's review of policy form -- or really more accurately, product -- regulation. First, if pre-market form regulation must remain in place as a general rule, the subcommittee should start with a market-friendly construct that will encourage insurance companies to innovate and provide consumers with a range

of policy options. An “informational filing” framework would provide such incentives. AIA and the Independent Insurance Agents and Brokers of America (IIABA) also have proposed federal preemption of state form approval laws more restrictive than “file and use” with a strict 30 calendar day review period based on specific statutory standards. Either one of these systems would represent a significant improvement over the current framework, provided that there was strong, enforceable preemption of anything more restrictive.

Second, as the subcommittee has suggested and the AIA-IIABA proposal envisions, government review of insurance policy forms must be based on clear standards. The best way to ensure that this principle is met is to look to specific state statutory law as the sole basis for review. States should not informally implement broad interpretations of state law to disapprove policy forms. Also, where a form is disapproved for broad “public policy” reasons, a national administrative process must be available to review the grounds for disapproval. National preemption cannot work without strong enforcement of the preemptive standard.

Third, commercial policy forms should not be subject to any state review or approval. All commercial policyholders, from small businesses to large conglomerates, deserve to be able to purchase insurance products tailored to their specific needs, and those products should be available without delay. Commercial policyholders and their insurers would benefit from the flexibility that market-based form regulation provides. That flexibility will spur innovation in commercial insurance products and allow policyholders to manage risk.

The subcommittee mentions limited review of policy forms for “sophisticated” commercial policyholders. We would urge the subcommittee to eliminate the distinction between so-called “sophisticated” and “unsophisticated” policyholders. The states’ experience with statutory efforts to distinguish between “large” or “sophisticated” commercial policyholders and all others has largely been a failure, with states reaching radically different conclusions about the criteria and thresholds needed to define an exempt commercial policyholder. Looking only at the annual premium criteria for states enacting exempt commercial policyholder forms laws, the thresholds vary from a high of \$250,000 to a low of \$10,000. In the states with higher annual premium thresholds, only a fraction of 1 percent of commercial policyholders qualify for the exemption. Even at the \$10,000 level, only about 10% of commercial policyholders are eligible for the exemption. Thus, even under the best circumstances, roughly 90% of commercial policyholders are subject to the current forms constraints. The subcommittee process should not result in picking winners or losers among commercial policyholders, but should make the benefits of free market competition available to all commercial insureds.

Turning to market conduct, the subcommittee’s objective is to ensure nationwide, uniform adoption of a consensus market conduct law. The National Conference of Insurance Legislators (NCOIL) Market Conduct Surveillance Model Law is frequently cited as the model that should be the basis for national adoption. However, there are a number of improvements that must be made before that model can work as a standard. Foremost among these needed improvements is a “domestic deference” requirement. Domestic deference occurs where the state regulator in the jurisdiction where the insurer

is domiciled takes the lead on conducting an examination, and other states where the insurer is doing business defer to the lead state. Such a system, currently used for insurer financial examinations, would greatly reduce the number of duplicative market conduct examinations and would reduce insurer costs. Attempts to achieve domestic deference through NCOIL and the NAIC have failed. National uniformity and consistency of market conduct regulation must start with domestic deference.

On the subject of company licensing, the subcommittee envisions a single point-of-entry system based on uniform state adoption of the Accelerated Licensure Evaluation and Review Techniques (ALERT) developed by the NAIC. We agree that reform is necessary to avoid the overlapping, inconsistent, costly, and burdensome licensing standards employed by the states today. It makes little sense for national and regional companies to go through the licensing process in multiple jurisdictions. ALERT may be the appropriate vehicle to achieve national, uniform standards, but this process must undergo scrutiny at the congressional level to ensure that ALERT's translation as a national standard is not accompanied by onerous requirements.

Ultimately, the subcommittee's goals for policy forms review, market conduct regulation, and company licensing only can be achieved through strong national enforcement of preemptive federal standards. It is unrealistic – and raises significant constitutional problems – to expect the states to enforce federal standards, let alone to enforce them in a uniform and consistent manner. The industry's experience with the Gramm-Leach-Bliley Act of 1999 (GLBA) supplies ample evidence of the need for national oversight and dispute resolution. While GLBA established federal privacy standards for financial institutions, with implementation left to the functional regulators of those institutions, and the NAIC unanimously adopted a privacy model regulation, states like California, New Mexico, and Vermont have departed from that NAIC model, forcing insurers to comply with varying privacy standards and enforcement mechanisms. Indeed, even those states that looked to the NAIC model did so in piecemeal fashion or departed from the model in different, sometimes significant, ways. This maze of differing and inconsistent privacy standards made national uniformity impossible and made enterprise-wide privacy compliance difficult and costly. More importantly, it has led to consumer confusion over privacy protections, generated largely by the continuing changes in laws and regulations across the 50 states and the District of Columbia.

In addition, GLBA's registered agent and broker provisions were supposed to provide reciprocity on producer licensing in at least 29 jurisdictions, with the NAIC certifying that it had met the conditions of those provisions. Despite certification, key states are still not in compliance. Even those that have been certified by the NAIC still allow variances – extra requirements like fingerprint and background checks – before a non-resident license is granted. Moreover, if Congress merely enacts standards with no accompanying federal enforcement mechanism, it is all but inevitable that day-to-day interpretations and other ongoing regulatory matters will either be decided in court or, by default, be brought back to the subcommittee. For these reasons, we strongly encourage a national enforcement mechanism that can resolve disputes over the application of preemptive standards.

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The subcommittee is tackling important and much-needed reforms in key areas of the state insurance regulatory system, and is to be commended for taking the initiative and inviting all constituencies to participate actively. Yet, reforms will only be worthwhile if they are bold, and are accompanied by an oversight mechanism that ensures national uniformity and consistency. A market-based regulatory system will eliminate needless paperwork and replace that red tape with efficient regulation that protects consumers by assuring that insurance companies are around when consumers need them most. Thank you for the opportunity to testify today, and I am happy to answer any questions the subcommittee might have.