



July 21, 2009

Dear Representative:

As Congress moves towards a debate over sweeping reform of the nation's financial regulations, we urge you to pay careful attention to public policy questions concerning insurance. Although we may differ on some of the details, all of us support the idea of a modern, streamlined, optional national regulatory system for property and casualty and life insurance. Through bureaucratic price controls, limits on innovation, and ill-considered regulations, the current system does not serve the needs of our national economy. An improved system, we believe, should give insurers and consumers the option of dealing with federal or state regulated entities. In so doing it would serve the needs of insurance consumers nationwide while improving our national economy.

As proposed in the National Insurance Consumer Protection Act (H.R. 1880), such a system of voluntary federal regulation—sometimes referred to as an optional federal charter—would have several advantages. We believe it would help American consumers, improve regulation of the insurance industry, and boost America's international competitiveness. We address these arguments in order.

Helping Consumers

A federal regulator would provide consumers with new products, insurance regulation that allows rates to reflect risk better, and a greater diversity of insurance choices.

To begin with, the property and casualty insurance products that American consumers buy to insure their homes and automobiles have not changed in a significant way in a half century. Young men and women starting families today buy the same products their grandparents purchased. The fragmented, inconsistent state regulatory system deserves a lot of blame for this situation. Each new product needs separate approvals in every state, territory and position of the United States. When, on occasion, insurers come up with modest innovations such as pay-per-mile automobile insurance and "accident forgiveness," they can take decades to become available nationally.

The current system for regulating insurance also charges rates that often fail to reflect risk. Because political factors predominate in many state's insurance decision making, cross subsidies have become extremely frequent. It is common for well-off coastal residents to receive implicit subsidies from those

who live inland, for male drivers to receive subsidies from female drivers, and for those who live in high-population density areas to receive subsidies from those who live in less dense areas. None of these cross subsidies has any basis in actual risk factors.

Finally, a more open and competitive insurance market would provide consumers with more competition for their insurance dollars. Today, many well-run insurance companies operate in only a few states rather than dealing with the hurdles of multi-state regulation. Likewise, insurance agents and brokers—trusted, general-purpose financial advisors—often have great difficulties following their consumers across state lines. This makes no sense. It should change.

Improving Regulation

The current fragmented system of insurance regulation often accomplishes the opposite of its stated goals. A federal system would allow for better policing of genuine cases of corporate fraud, improve oversight, and improve systemic stability of the American economy.

Like all large companies, sizeable modern insurers are holding companies that collect many subsidiaries and assorted legal entities under a single banner. AIG, until recently the world's largest insurer, had nearly 80 U.S.-based subsidiaries and over 1,500 legal entities worldwide. State insurance regulators are not equipped to handle companies of this size. In AIG's case, these structures made it easier for things to go seriously wrong.

A federal regulator, properly constructed, could focus on genuine efforts to prevent fraud in the insurance industry. Rather than focusing on issues of rates and product approvals—decisions better made through private bargaining and market mechanisms-- it could become a vigorous force to prevent, discover, and punish wrongdoing. This would discourage underhanded, illegal, and questionable actions while strengthening the hands of honest players.

The current system of state regulation appears to have encouraged instability by allowing states to set insurance prices by government fiat without regard to the broader implications of this price fixing. These government-set prices both destabilized companies.

Strengthening Competitiveness

America's dated insurance system hurts our international competitiveness. Data from the Organization for Economic Cooperation and Development (OECD), comparisons of the United States' system those in other developed nations, and the evolving structure of EU regulation all suggest that our system needs to change.

While parsing out insurance sector productivity data is a difficult task, OECD data appears to indicate that the United States has a distinctly uncompetitive Finance, Insurance, Real Estate sector. While our productivity leads the world in nearly all other major economic sectors, our FIRE productivity lags behind. Our fragmented insurance system plays a role in this.

All other major economic powers have some form of national insurance regulation. In countries like The United Kingdom and Japan, national governments perform almost all insurance regulation. In Canada and Germany, the two other G-8 countries with federal systems, likewise, forms of federal regulation exist alongside regulation at the province/*lander* level.

Finally, the European Union has begun efforts to integrate its insurance market. A degree of “mutual recognition” for insurers already exists between all of the EU’s 27 members. The implementation of the Solvency II standards will create a largely integrated Europe-wide insurance market. U.S.-based insurers may have a difficult time competing unless our system meets the EU’s equivalent standard at the national level.

Closing Thoughts

The idea of an optional federal charter deserves your careful consideration. It is not a liberal idea or a conservative idea. It is simply a matter of common sense and good, prudent regulation. We urge you to give it due consideration.

Yours truly,

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