

COMMENTS
OF
AMERICAN INSURANCE ASSOCIATION
ON
THE JOINT FORUM'S PRINCIPLES FOR THE SUPERVISION OF FINANCIAL
CONGLOMERATES
CONSULTATIVE REPORT
(DECEMBER 2011)

The American Insurance Association represents companies that write property and casualty insurance throughout the world. Therefore, we much appreciate the opportunity to comment on the Joint Forum's "Principles for the supervision of financial conglomerates." Accordingly, we are pleased to provide our comments, below, and incorporate by reference comments submitted by the International Network of Insurance Associations, in which we participated.

General Comments

As a basic premise, we believe that consumers are best served by effective and efficient regulation that assures: there are no regulatory gaps; duplicative or contradictory regulation/supervision is avoided; all supervisors have clear roles and responsibilities; supervisory coordination and cooperation and confidentiality protection are adequately provided and the legal rights of insurers are respected so as to encourage and support competition. Further, all supervisory and regulatory processes should be consistent with the OECD's Policy Framework for Effective and Efficient Financial Regulation; however, legal and cultural differences in the various jurisdictions need to be respected. Principles should not be put forth if they are unlikely to be adopted by those jurisdictions.

2. Objective

We believe that the notion of efficiency should be included as an objective. This would be consistent with other supervisory standards, such as the Insurance Core Principles and the work of the OECD.

Corporate Governance.

Corporate governance standards need to be consistent with the legal and regulatory environment of the various jurisdictions in which they would be applied. For example, the idea of regulators having the unfettered right to replace corporate officers and directors would not fit well in certain jurisdictions, including the United States. Additionally, we are concerned about ambiguous and subjective definitions of “suitability”. Because replacing corporate directors or officers is such a draconian regulatory measure, it should be carefully and narrowly defined, if it is a power that regulators are to have. And, there should be guaranteed rights on the part of the individuals and the company to contest regulatory direction and a right of appeal.

3. Scope of application

Supervisory oversight

We agree with the need for flexibility so as to be able to implement the principles in different jurisdictions. We also support the notions set forth in this section of: a strong and singular group supervisor, transparent supervisory processes, clear roles and responsibilities among supervisors and effective mechanisms for resolving differences among supervisors.

Principles

1. Comprehensive group-wide supervision

Implementation criteria 1(b) contains an undefined suitability standard for ownership. Again, we have serious concerns about potential abuse of this power unless it is carefully limited to objective criteria and there is the right to appeal supervisory direction.

Implementation criteria 1(c) mentions “a sufficiently transparent group structure so as to not impede effective supervision...” If this implies that the supervisor has the ability to discuss issues relating to corporate structure with the company, this provision is acceptable. On the other hand, if it implies that the supervisor has the authority to compel restructuring of a well functioning company, we challenge it as an inappropriate intrusion into company management and a dangerous blurring of the lines between the regulator and the regulated entity.

2. Cooperation and exchange of information

We strongly support the **implementation criteria's** language on confidentiality protection.

3. Independence and accountability

We strongly support the principles of supervisory accountability and independence. We endorse especially the **explanatory comments** language that: "Supervisors should also be subject to clear and public objectives and accountable for the discharge of their duties."

5. Group-level Supervisor

We strongly support this principle and the Implementation criteria, with emphasis on the need for a single Group-level Supervisor and cooperation and coordination among relevant supervisors.

6. Supervisory cooperation, coordination and information exchange

We strongly endorse the **implementation criteria 6(a)** which provides for clarification of objective, roles and responsibilities of each supervisor, **6(b)** which provides for clarification of arrangements for information flows, **6(f)** which relates to legal restrictions and the need to protect confidentiality and **6(g)** which provides for arrangements for resolving disputes among supervisors. We also support all of the explanatory comments.

7. Prudential standards and coverage

There are significant impediments to implementing global capital standards. For example, different legal and regulatory environments, coupled with uneven enforcement and different interpretations of those standards, will likely result in substantial variances in application and outcome. As a result of these issues, the concept of global capital standards and alternatives is being intensively debated at IAIS. Accordingly, this principle therefore should remain at a very high level, at this time.

9. Supervisory tools and enforcement

This principle and its implementing criteria should include requirements that levels of intervention and the grounds for acting on them should be clearly spelled out in the law and the law should provide companies a right of appeal. The absence of these guarantees is a fundamental flaw in this paper.

10. Corporate governance in financial conglomerates

Explanatory comment 10.1 mentions “suitability of board members, senior management, key persons in control functions and significant owners”. We raise again serious concerns about a lack of a clear and objective definition of suitability and the danger of abuse without a right of appeal.

11. Structure of the financial conglomerate

It is not clear if the principle and **implementation criteria (e.g. 11(b))** stand for the proposition that a supervisor can order a company to restructure. If so, we believe it is a dangerous incursion into the appropriate role and rights of the regulated entity. On the other hand, **explanatory comment 11.1** appropriately states that: “ A financial conglomerate may freely set its...organization.”

12. Suitability of significant owners, board members, senior management and key persons

The principle and related materials define suitability in terms of “integrity, competence, experience and qualifications...” to “...exercise sound objective judgment”. These standards are, in our view, far too ambiguous and subjective, considering the immense power given to supervisors through “suitability” determination. Not only are the standards problematical but there is no legal due process under which an individual or a company could contest a ruling of unsuitability. It would be far better to define suitability as the absence of objective, disqualifying activity such as fraud or other criminal activity. The section is improved slightly, however, by the statement in **explanatory comments 12.6** that: “Competence can generally be judged from the level of professional or formal qualifications.”

15.-20. Capital adequacy

This is currently a much debated and discussed issue in insurance regulation. Until that is resolved, we are reluctant to endorse any particular approach to group capital requirements. At the very least, group capital mandates should not duplicate capital already held by subsidiaries and should cover only risks at the group level not otherwise covered by subsidiary capital.

Although **Principle 19** acknowledges that group capital may not be fungible, the existence of an overall group capital requirement presumes that capital is fungible. If capital cannot be freely moved among jurisdictions, particularly in response to financial stress, there is no benefit to a group capital requirement.

A more practical (and useful) approach may be to require a group capital assessment by an insurer as part of its enterprise risk management process.

21-29. Risk Management

Over-all, we are concerned about new group level reporting and the increased involvement of supervisors in company management. For example, **Principle 24. New business**, seems overly intrusive. If the over-all risk management system is acceptable, supervisory power to veto individual market/business decisions should be avoided.

Conclusion

We greatly appreciate the opportunity to comment. As noted, there are some very good provisions, including confidentiality protections, and the need for clear roles and responsibilities for all supervisors. Conversely, there are provisions that we feel cross the line between regulating a company and managing it, including suitability, approval of new business and sanctions without a right of appeal. Finally, the capital adequacy provisions, in particular, seem premature as they relate to insurance supervision when group capital issues for insurance are under intensive discussion currently and there is not yet a consensus among insurance supervisors.

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