ASSESSING THE U.S.–E.U. COVERED AGREEMENT

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND INSURANCE

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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WITNESSES

THURSDAY, FEBRUARY 16, 2017

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

ASSESSING THE U.S.–E.U. COVERED AGREEMENT

Thursday, February 16, 2017

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING AND INSURANCE,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:07 a.m., in room 2128, Rayburn House Office Building, Hon. Sean P. Duffy [chairman of the subcommittee] presiding.

Members present: Representatives Duffy, Ross, Royce, Pearce, Posey, Luetkemeyer, Hultgren, Rothfus, Zeldin, MacArthur, Budd; Cleaver, Velazquez, Sherman, Lynch, Beatty, Kildee, Delaney, and Kihuen.

Ex officio present: Representative Hensarling.

Also present: Representatives Green and Heck.

Chairman DUFFY. The Subcommittee on Housing and Insurance will now come to order. Today's hearing is entitled, "Assessing the U.S.–E.U. Covered Agreement."

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Also, without objection, members of the full Financial Services Committee who are not members of the subcommittee may participate in today's hearing for the purposes of making an opening statement and questioning the witnesses.

The Chair now recognizes himself for 4 minutes for an opening statement.

I first want to welcome our members to the first hearing of the Housing and Insurance Subcommittee in the 115th Congress. I am pleased to have the opportunity to work with Mr. Cleaver, our ranking member, and my vice chairman, Mr. Ross. We have a full agenda this year, including reauthorization of the National Flood Insurance Program, GSE reform, and many other priorities.

I had not intended our first hearing to be on the U.S.-E.U. covered agreement, but given the 90-day layover period, which just began a month ago, it is our duty to study the agreement, to solicit feedback from the insurance industry, to assess its impact on policyholders, and ultimately, to weigh in on its merits.

I have been listening to many stakeholders, some of whom we will hear from today, about the merits and the demerits of this agreement. Those points notwithstanding, I must say that I come from a place of a skepticism over this agreement that was signed or put into effect on Friday the 13th with just 1 week left in the

Obama Administration. I would also remind those in the room that the centerpiece of Donald Trump's campaign for President was negotiating better international deals.

There is no doubt in my mind that President Trump's election weighed heavily on European and American negotiators to get a deal done before he took office. The President and his new Treasury Secretary should be afforded the chance to decide for themselves whether to renegotiate or to sign this deal.

Furthermore, I believe the committee should consider improvements to international insurance negotiations, to enhance the role of State insurance regulators like Commissioner Nickel, and the role of Congress in that process. This committee has had an interest in international insurance negotiations for some time and has expressed concerns about transparency and the potential for state-based regulatory systems to be undermined.

I would also note that there has been bipartisan attention paid to this matter, and I commend Mr. Heck for all of the work he did last year to protect our State-based system. So to be blunt, I think a 90-day layover is an insult to this institution and does nothing more than pay lip service to the notion of congressional consultation and input.

In the E.U., it is my understanding that there will be at least two affirmative votes to approve this agreement. In the U.S., Congress will have no affirmative votes on this deal, much less an ability to easily disapprove of it if we decide to pursue that course of action.

So I look forward to working with my colleagues in a bipartisan fashion on this subcommittee to address this issue.

I now want to recognize my colleague from Florida, the Vice Chair of the subcommittee, Mr. Ross, for 1 minute.

Mr. ROSS. Thank you, Mr. Chairman. And thank you for holding this important hearing.

The U.S. insurance market is the largest and most vibrant of any nation in the world. Our market is strongly regulated by the States, putting an emphasis on the protection of policyholders. I support this system of regulation, which has existed for nearly 150 years. In the global insurance marketplace, however, regulatory systems vary. Recently, the E.U. implemented a directive that has created market access barriers for the U.S. insurers. This harms U.S. businesses and is a problem for our domestic companies and must be addressed.

Today, we will discuss the covered agreement negotiated between the U.S. and the E.U. Ultimately, when I analyze the covered agreement, I am focused on its impact on consumers and policyholders. I want to know how this agreement will impact the homeowners and families in my district and the crop insurance premiums of those citrus growers across Florida. I look forward to the testimony today and I yield back the balance of my time.

Chairman DUFFY. The gentleman yields back. It is now my pleasure to recognize the ranking member of the subcommittee, the gentleman from Missouri, Mr. Cleaver, for 5 minutes for an opening statement.

Mr. CLEAVER. Thank you, Mr. Chairman. And I look forward to working with you on a number of critical issues. This is, of course, just one. And our vice ranking member, Dan Kildee, is also here today and will play a major role in whatever we are able to get going to the benefit of the country.

I remember that under Title V of the Dodd-Frank Act, this hearing is supposed to take place along with a consultation. And I see the covered agreement as something that enhances and protects U.S. insurance consumers and increases, in my estimation, opportunities for U.S. insurance companies and reinsurers.

Today, it gives us an opportunity to assess the finalized covered agreement that has been reached between the U.S. and the E.U. regarding international insurance and reinsurance issues. The Federal Insurance Office (FIO) and the United States Trade Representative (USTR) announced their intention to move forward with the negotiations in November of 2015. A final agreement was reached on January 13th of this year and a copy of the text was submitted to the relevant congressional committees, beginning a 90-day layover period. No further action from Congress is required for this agreement to go into effect.

The covered agreement focuses on three areas of prudential supervision: reinsurance collateral; group capital; and exchange of information between supervisory authorities. As we all know, on January 1, 2016, the E.U. began to implement its insurance regulatory scheme, commonly known as Solvency II, and U.S. reinsurance companies began to be subjected to burdensome and expensive E.U. standards as our system was not equivalent to that of the Solvency II system.

The covered agreement works to address this issue and will allow U.S. reinsurance companies to be able to continue to operate in the E.U. without costly new obligations. Additionally, the covered agreement recognizes the U.S. State-based system. And of course, having made a commitment a long time ago, I would never do anything, say anything or support anything which would damage our State system. I think it has been an integral part of our system of insurance and I will do everything that I can to make sure it stays that way.

So I am hopeful that this agreement will provide certainty for our insurance system and enhance consumer protection. I know there are a number of questions regarding this covered agreement, and I look forward to hearing them answered today. Thank you, Mr. Chairman.

Chairman DUFFY. The gentleman yields back. I now want to welcome our panel, our witnesses for today's hearing. Thank you for being here.

I first want to introduce Mr. Michael McRaith. In 2011, Mr. McRaith was appointed as the Director of the Federal Insurance Office by former Treasury Secretary Tim Geithner, where he served until last month. He is now appearing as a private citizen. Mr. McRaith was integral to the negotiation of the covered agreement that we are now here to discuss, so we are grateful for his appearance. Immediately prior to his appointment as FIO Director, Mr. McRaith served more than 6 years as the Director of the Illinois Department of Insurance.

Next, from probably the greatest State in the Nation, Wisconsin, Commissioner Ted Nickel was appointed by Governor Scott Walker as Commissioner of Insurance for the State of Wisconsin in 2011. In December 2016, Commissioner Nickel was elected as President of the National Association of Insurance Commissioners. Commissioner Nickel is also a member of the National Association of Insurance Supervisors. And in 2014, he was appointed to the Federal Advisory Committee on Insurance, which serves as an advisory committee to the Federal Insurance Office.

Commissioner Nickel has been actively engaged in the insurance industry affairs in Wisconsin. Prior to his appointment, Commissioner Nickel worked for almost 18 years as Director of government and regulatory affairs for Church Mutual Insurance Company in Merrill, Wisconsin. So I am proud to call Commissioner Nickel a friend, but also a constituent. No bias from the chairman here.

Next, I want to recognize Ms. Leigh Ann Pusey. Ms. Pusey is the president and CEO of the American Insurance Association (AIA). AIA is the leading property and casualty insurance organization, representing more than 325 insurers that write more than $127 billion in premiums each year. A veteran of the insurance industry, Ms. Pusey joined AIA in December of 1996 and was elevated to president and CEO in February of 2009.

And finally, I want to introduce Chuck Chamness, who serves as president and CEO of the National Association of Mutual Insurance Companies, or NAMIC, a 1,400-member company property and casualty insurance trade association. Mr. Chamness served in the first Bush Administration as Deputy Assistant Secretary for Public Affairs under HUD Secretary Jack Kemp, before being named to his current position in 2003.

Now, the witnesses will each be recognized for 5 minutes to give an oral presentation of their testimony. And without objection, the witnesses' written statements will be made a part of the record.

Once the witnesses have finished presenting their testimony, each member of the subcommittee will have 5 minutes within which to ask questions of the witnesses.

On your table, you will note there are three lights: green means go; yellow means you have 1 minute left; and red means your time is up.

And with that, I now recognize Mr. McRaith for 5 minutes for his opening statement.

STATEMENT OF MICHAEL T. MCRAITH, FORMER DIRECTOR, FEDERAL INSURANCE OFFICE (FIO), U.S. DEPARTMENT OF THE TREASURY

Mr. MCRAITH. Chairman Duffy, Ranking Member Cleaver, and members of the subcommittee, thank you for inviting me to testify. I appear on my own behalf as the former Director of Treasury's Federal Insurance Office and as Treasury's lead negotiator for the covered agreement.

First, thanks to Commissioner Nickel and his colleagues for the integral role they played in the negotiations. We created an unprecedented mechanism for State regulators to join our delegation, and they attended and participated in person in every negotiation except the final one in Brussels, which they joined by telephone.

Through a confidential Web portal, State regulators received every E.U. document shortly after it arrived, and before any U.S.

document was sent to the E.U., we shared it with the States and then held a conference call with them to receive their feedback. State regulators were an essential part of our delegation.

The issues addressed by the agreement are not new. Reinsurance collateral reform and Solvency II implications have been discussed in the U.S. for years. The agreement brings closure to these issues. While the States have undertaken to reform reinsurance collateral requirements, reform that benefits E.U. reinsurers, the States received nothing of benefit for the U.S. industry. Nothing.

Through the agreement, U.S. reinsurers now have access to the entire E.U. market on the same terms as E.U. reinsurers operating in the U.S. With respect to U.S. insurer groups, the agreement caps the application of Solvency II to the E.U. operations of U.S. insurers. To repeat: The agreement affirms that the U.S. supervises its insurance sector as the U.S. deems appropriate. This outcome saves our insurers potentially billions of dollars, preserving American jobs and benefiting U.S. industry and consumers.

States have been developing a group capital calculation for more than 2 years. The agreement, which applies only to those insurers operating in the E.U. and the U.S., does not prescribe the content of that calculation and does not even imply that States should create a holding company capital requirement. That notion, a complete fiction, would completely contravene the entire purpose of the agreement. The agreement endorses States for what they do, or in the case of group capital, what they have publicly committed to do, and gives them 5 years to do it.

The agreement is cross-conditional. Neither the E.U. nor the U.S. receives the benefits without satisfying the conditions. And if a question arises, the agreement provides for the resolution. If both sides satisfy the conditions within the 5-year period, then the terms of the agreement become permanent, final.

We entered into the negotiations seeking to improve the rigor, uniformity, and consumer protections of U.S. reinsurance oversight. We sought to endorse the U.S. system. We sought to include the U.S. State regulators in a manner without precedent in American history. We achieved these goals.

We sought to remove excessive regulation that neither protected consumers nor supported industry. We sought to ensure that U.S. insurers operated in the E.U. on a level playing field. We achieved these goals, saving our industry potentially billions of dollars. While providing equal benefits to the E.U., this covered agreement puts America first. Our diverse U.S. insurance sector will no doubt always include skeptics, but this is not a time for our predictable debate. This is not a theoretical discussion about concepts or statutory prerogatives. This agreement answers real-time questions about the allocation of capital by U.S. insurers, about business opportunities for U.S. insurers and reinsurers, and whether U.S. industry operating in the E.U. employs more Americans or fewer.

Will U.S. industry grow or will it be stifled? Some will continue to conjure up the elaborate fictions, but now is the time to skip the usual script, to see the real threat to U.S. insurers' growth and the threat to insurance jobs in States around our country, and to show American leadership. Now is the time to solve a real problem, and this agreement does just that.

Thanks for your attention. I look forward to your questions.

[The prepared statement of Mr. McRaith can be found on page 49 of the appendix.]

Chairman DUFFY. Thank you. Commissioner Nickel, you are now recognized for 5 minutes.

STATEMENT OF THE HONORABLE TED NICKEL, COMMISSIONER, OFFICE OF THE COMMISSIONER OF INSURANCE, STATE OF WISCONSIN, ON BEHALF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS (NAIC)

Mr. NICKEL. Thank you, Chairman Duffy. Chairman Duffy, Ranking Member Cleaver, and members of the subcommittee, thank you for the opportunity to testify here today.

The NAIC is very concerned with the disparate treatment some E.U. jurisdictions are imposing on U.S. insurers and is committed to working with Congress and the Administration to address this important issue. While a covered agreement is one way to resolve these issues, we oppose this one. We urge Congress and the Administration, with direct involvement of the States, to expeditiously reopen negotiations with the E.U. to reach an agreement which brings finality to these issues and better protects U.S. consumers, insurers, and the State regulatory system.

While we recognize that the United States received some benefits, including the apparent elimination of the local presence requirements, the current agreement does not provide for full equivalence or recognition of our regulatory system. In fact, the word "equivalence" is nowhere to be found in this document.

This agreement places conditions on the ability of regulators to obtain information or to take certain actions currently authorized under State laws. There are potential conflicts between this agreement and State reporting processes, as well as critical examination and hazardous financial condition authorities.

The group capital provisions imply State regulators are required to adopt a group capital requirement, but also include language suggesting the E.U. could apply its own group capital requirements and reimpose local presence requirements if the States choose not to act or fail to meet E.U.'s expectations. This is not a win for the U.S. insurers and consumers who will have to absorb these costs.

This agreement does not include any evaluation of the creditworthiness of foreign reinsurers backing up U.S. risks. The Treasury Department had committed that it would never wipe out insurance collateral, yet it did just that. Collateral protects U.S. insurers and consumers from counterparty risk. More than $30 billion of E.U. reinsurer collateral is eliminated by this agreement. Absent that protection, regulators will likely have to find other mechanisms with which to protect insurers and your constituents from the risks posed by those counterparties.

This agreement is also littered with ambiguities to be resolved by an undefined and unaccountable joint committee, leading to perpetual renegotiation and uncertainty. In a single agreement with an outgoing Administration, the E.U. achieved its primary objective of eliminating collateral requirements.

In return, U.S. companies and our regulatory system received a form of probation which could be revoked at any time. The burden for this is placed almost entirely upon the States, with its underlying costs ultimately paid for by the U.S. insurers and consumers.

These defects should be no surprise. This flawed document resulted from a flawed process. Unlike a trade agreement, there was no formal consultation with U.S. stakeholders. Despite assurances to the contrary, the few of us in the room were merely observers subject to strict confidentiality with no ability to consult with our fellow regulators. The process favored the E.U., which retains the European Parliament's and Council's ability to approve the agreement, whereas the U.S. has virtually no comparable congressional authority. This agreement sets a precedent that others around the world may try to imitate, and forces the U.S. to weaken our standards in exchange for very little.

Going forward, we would like the Administration to establish a transparent process for negotiating and allowing more robust congressional and stakeholder engagement and providing meaningful and direct participation by all impacted insurance regulators.

In terms of specific substantive improvements, the new agreement should provide for permanent mutual recognition, equivalence, or comparable treatment for U.S. firms operating in the E.U. It should recognize the U.S. regulatory system, including group supervision and capital, provide clarity in the agreement's terms, and finality in its application.

In conclusion, we are committed to working toward an agreement which is truly in the best interest of the U.S. and brings closure to the issue of equivalence, but this is not such an agreement. Thank you, Mr. Chairman, and with that, I would be pleased to answer any questions.

[The prepared statement of Commissioner Nickel can be found on page 59 of the appendix.]

Chairman DUFFY. Thank you, Commissioner. Ms. Pusey, you are recognized for 5 minutes.

STATEMENT OF LEIGH ANN PUSEY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AMERICAN INSURANCE ASSOCIATION (AIA)

Ms. PUSEY. Thank you, Chairman Duffy, Ranking Member Cleaver, and subcommittee members. I appreciate the opportunity to testify today on behalf of our member companies. This is a tremendously important issue to the insurance industry, and it really needs immediate attention.

I can't tell you how I hate to have to disagree with Commissioner Nickel and our leadership at the NAIC. But on this issue, we really see it very differently. We see this as a real win for insurers, for U.S. insurers.

This was a win not only for companies operating in the U.S., but for our regulatory system. And for that matter, for our consumers, who are going to continue to be protected because all the provisions of the U.S. regulatory system are carried forward in this agreement.

As the ranking member articulated in his opening comments, we all know what the problem is. We have U.S. insurers operating in the European Union who are being discriminated against today. And this was a result of the implementation of Solvency II over there, so whether it was in the U.K. or in the E.U., they were beginning to require things of our primary insurers operating there and their subsidiaries of their branches. They were requiring us to—they were basically enforcing Solvency II upstream into the holding company, requiring everything from corporate governance rules of the E.U. to reporting requirements to capital requirements that could be enforced back onto the U.S. parent, because that was the way they were reading Solvency II.

For the reinsurance community, and again, as the Director pointed out, this was not a new issue, but what was increasingly difficult on the collateral front was that there was a reaction in Europe and they were beginning to require reinsurers to have a physical presence in the E.U. to do business there. Again, a discrimination which was not something they were requiring of their own companies.

So for us, we saw this agreement as timely and a win. It was a win for the U.S. insurance industry because no longer can they export Solvency II requirements upstream to the U.S. holding company. That is huge. It is a recognition of our State-based regulatory system. It will also eliminate this requirement for reinsurers to have a physical presence in the E.U. in order to compete.

For U.S. insurance consumers, as I just mentioned, we believe this continues to be a win, because it is not only going to bring forward the protections that are in U.S. law, but they will also, we believe, increase competition, which we think is also good for consumers to having more choices.

For the U.S. insurance regulatory regime, we see this as a big win. It provides really historic recognition and respect for the U.S. insurance regulatory system in an international agreement. That has never been done before.

And with respect to group capital, it relies on existing authority without demanding any specific capital requirement, and it carefully references the group capital calculation effort already under way at the NAIC.

With respect to collateral, it utilizes existing NAIC rules and even builds the language into the agreement. We take those prescriptions from NAIC's model law, and they are put into this covered agreement. I would say that we are not taking collateral. In practical effort, in 2011 when the NAIC began to—they agreed to a model law on collateral and it began to move its way through the States, and it is approved in 35 States, it reduces effectively collateral from 100 percent which AIA used to support, but under this new model that we all agreed to support, it will effectively reduce it to around 20 percent on average.

So this is not going to eviscerate U.S. collateral rules. In fact, it builds on what the NAIC is already doing. It just helps us get there in a more uniform way, and it has a unique approach for E.U. reinsurers. That is true. But again, it is not eviscerating collateral. And all the rules and protections around collateral, the ability to require timely payments, the ability to negotiate additional requirements for collateral around your agreement, these are—and to require prompt payment, all of those things were carried forward into this agreement.

For U.S. negotiators, we haven't talked about this, but as this committee knows well in your efforts, we have all been involved for many years now at the international level, at the IAIS, as well as, quite frankly, at the FSB on insurance global matters. And for our negotiators, they will be in a very strong position empowered by this agreement, because now we have the E.U., the second largest market, recognizing our regulatory system and our capital standards, and we are going to go into those negotiations much stronger off, we believe. So we believe it is a win.

We acknowledge that the process could be improved. We would fully support efforts to review efforts to be more transparent and inclusive. We were among the earliest to call for a robust role for the NAIC. So we would look forward to that.

Let me wrap up quickly. We think this is a win. And the only concern we have with scrapping this deal is we believe there is no guarantee that we would have a timely result that can affect our companies today. What is going to take the place of this agreement for U.S. companies that are currently being discriminated against in Europe if we don't do this? Thank you, Mr. Chairman.

[The prepared statement of Ms. Pusey can be found on page 66 of the appendix.]

Chairman DUFFY. Thank you. And the Chair now recognizes Mr. Chamness for 5 minutes.

STATEMENT OF CHARLES CHAMNESS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES (NAMIC)

Mr. CHAMNESS. Good afternoon, Chairman Duffy, Ranking Member Cleaver, and members of the subcommittee. Thank you for the opportunity to speak with you today. My name is Chuck Chamness, and I am president and CEO of the National Association of Mutual Insurance Companies (NAMIC).

NAMIC is the largest property-casualty insurance trade association in the country, with more than 1,400 member companies representing nearly 40 percent of the insurance market. We appreciate the subcommittee's focus on assessing the impact of the recent U.S.-E.U. covered agreement. As the first of its kind, this bilateral agreement with the authority to preempt existing State insurance law merits careful scrutiny to understand its impact on the U.S. domestic insurance industry and policyholders.

Let me start by saying that NAMIC has long had serious concerns about the use of an international trade agreement and negotiation process to alter or preempt State-based insurance regulation. This final draft covered agreement validates our long-held concerns.

We also believe that the covered agreement does not address the problems the FIO and the USTR committed to resolve when the negotiations were started, and the agreement represents a bad deal for the U.S. domestic property-casualty insurance industry.

First, in announcing the negotiations, the FIO and the USTR sent a letter to Congress outlining their objectives. Chief among them was to obtain permanent treatment of the U.S. insurance regulatory system as equivalent by the E.U. This had become an issue due to last year's implementation of the E.U.'s insurance regulatory reform known as Solvency II.

Under the new regime, an insurer doing business in the E.U. will have heightened regulatory requirements in the event the insurer's country of domicile is not deemed equivalent for purposes of insurance regulation. This created a real and present difficulty for the relatively small number of U.S. insurers doing business overseas.

It also provided an opportunity for the E.U. to push for something it had always wanted for reinsurers, its reinsurers, that is: the elimination of requirements on foreign reinsurers to post collateral in the U.S. The covered agreement was seen as a vehicle to resolve both issues.

To be clear, NAMIC strongly supports U.S. insurers doing business overseas, and we are fundamentally opposed to the unfair trade barriers the E.U. is attempting to erect. It is important to remember that the equivalency determination is an entirely contrived problem of the E.U.'s manufacture. That determination is being used simply as a source of pressure on the U.S. to continue to alter its regulatory system to the E.U.'s liking.

Even if we were to stipulate that equivalence was a real problem and that the covered agreement and forfeiting reinsurance collateral were necessary to solve it, the agreement fails on its own terms. There is no finding anywhere in the covered agreement that the U.S. group supervision is adequate, mutual, or equivalent.

Instead, it merely calls for the E.U. to return to the pre-Solvency II status quo of not unfairly punishing U.S.-based insurers. Nor is there any guarantee that this status quo will continue at the end of the agreement's 5-year term. Even the Treasury's own summary of the agreement provides that continuation of this accord between the U.S. and the E.U. is merely an expectation, not a commitment.

This lack of commitment, coupled with the establishment of a joint committee with the power to amend the agreement, will likely lead to a process of endless renegotiation with the E.U. when the E.U. decides it would like to see further changes in the U.S. system.

Of perhaps greatest concern is the requirement for a new group capital standard for all U.S.-based insurance groups. If these group capital standards are not adopted, the E.U. will not live up to its side of the agreement, but if they are adopted, it will impact even those companies not doing business in the E.U. This provision is at odds with the U.S. legal entity system of regulation.

The agreement also states that the U.S. group capital standard must apply to the complete "worldwide parent undertaking," and include corrective or preventative measures up to and including capital measures. It seems to include the power to require increases in capital, capital movement between affiliates, or other fungibility mandates.

Implementation of this kind of group capital standard will shift the U.S. from a legal entity regulatory system that protects policyholders towards an E.U.-style group supervision system designed to protect investors and creditors. This would not be a win for U.S. policyholders.

The 2015 letter announcing negotiations with the E.U. clearly stated that Treasury and the USTR will not enter into a covered agreement with the E.U. unless the terms of that agreement are beneficial to the United States. NAMIC does not believe this agreement meets that criteria.

On the whole, it is bad for the vast majority of U.S. insurers which do not have operations in Europe and which lose reinsurance collateral and get nothing in return other than new group supervision and future regulatory uncertainty.

We urge Congress to work with the Administration to reject this agreement and work on a new solution that meets the needs of the U.S. insurance industry and the insurance-buying public.

Again, thank you for the opportunity to speak here today, and I look forward to answering any questions you may have.

[The prepared statement of Mr. Chamness can be found on page 40 of the appendix.]

Chairman DUFFY. The gentleman yields back.

I want to thank our witnesses for their opening statements. The Chair now recognizes himself for 5 minutes for questions.

Commissioner Nickel, I don't know if you heard Mr. McRaith testify that you were able to attend and participate in this great deal that puts America first. Do you agree with that assessment?

Mr. NICKEL. There was a small band of brothers of insurance commissioners who were put together to be a part of the process, that is correct. We were allowed to participate in various forms throughout the negotiation, as Mike clearly stated. I suspect we will have some different arguments today about the process. Unfortunately, the content of the meetings I can't discuss, because I am bound under strict confidentiality.

And the most difficult part of—

Chairman DUFFY. Even now?

Mr. NICKEL. Yes.

Chairman DUFFY. You can't tell Congress?

Mr. NICKEL. I don't think I can tell anybody, unless somebody gives me the authority to do that. But the most difficult part about that process was I was even bound from speaking with my own legal counsel, my own chief financial people, so you can imagine—put yourself in those shoes, where you are trying to understand something about which you can only talk to this small cadre of your fellow commissioners.

Chairman DUFFY. You were given active input in consulting continuously with Mr. McRaith, taking the ideas that you had, the concerns that you had into consideration as this deal was negotiated?

Mr. NICKEL. We were sharing our thoughts and opinions with Mr. McRaith and his team.

Chairman DUFFY. Okay. Were your thoughts and concerns, do you think, heard and taken into consideration as this deal was negotiated?

Mr. NICKEL. I would say, to be fair, Mr. Chairman, that some of our input found its way into the agreement. Quite a bit of it probably did not, which is why I am here today, because the membership of the NAIC, all 56 members, came to the conclusion that this deal was not a good deal for the U.S. regulatory system, consumers, and insurers.

Chairman DUFFY. Thank you. I want to move to you, Mr. McRaith. I think in your written testimony you said, "The covered agreement does not need to be clarified with further written materials. This would be a fool's errand. The covered agreement terms painstakingly negotiated are abundantly clear, even if not written, to resolve every stakeholder's nuanced fantasies."

I have had a number of meetings—colorful language, by the way; it was good—with those who support and those who disagree with this agreement, and almost everyone agrees that there is a lack of clarity here. And even those who agree there is a lack of clarity, said that they might be concerned about how much time it would take us to get clarification, and they don't want to see the deal be torpedoed, but everybody has come together and said that there is a need for clarification, and it gives me pause that you are in essence saying, "No, not at all; it is crystal-clear."

The lawyers who have represented all the companies that are here today have basically given us the same feedback. One commonly cited portion is Article 4A, which lays out capital assessments as a lack of clarity. So what happens if the States create a capital standard that the E.U. disagrees with? Is that specified in the agreement?

Mr. MCRAITH. First of all, I appreciate you reading my testimony and the colorful prose is mine. And obviously, it is a reflection of the fact I don't have to clear this through the Treasury Department any longer.

Chairman DUFFY. Duly noted.

Mr. MCRAITH. As someone who practiced law for 15 years—and I say this with great respect and affection for the lawyers—it doesn't surprise me that people who have a perspective and angle they are pursuing would have lawyers who would support that perspective and angle.

What the agreement does is, it is absolutely clear on capital and group supervision that nothing is expected of the States other than what they have already said they will do.

Chairman DUFFY. I only have a minute. So what happens if the States create a capital standard that the E.U. disagrees with? Is that clear in there?

Mr. MCRAITH. The agreement is clear that it can be developed however the States want. It does not require anything other than what the States have already said they will do.

Chairman DUFFY. Then what happens if the E.U. disagrees? If the E.U. disagrees, how is that resolved? And where is that in the agreement?

Mr. MCRAITH. The agreement establishes a process, like every international agreement, questions about interpretation and implementation, if there is a question, we will meet and we will work it out and sort it out. It is entirely common practice.

Chairman DUFFY. All right, I have to be quick. So if it is not clear, it will be determined by a body that will be put together. And on the committee, who is going to represent the U.S. on the joint committee?

Mr. MCRAITH. Good question. One thing we did not want to do was—

Chairman DUFFY. No, no, I want to—you said, "We are clear on how this thing is going to work."

Mr. MCRAITH. That is right.

Chairman DUFFY. Where is the clarity of who is representing the U.S.? We don't know.

Mr. MCRAITH. The joint committee—it would depend on the issue. If it is an issue, for example, concerning a Wisconsin company, my expectation is that the Wisconsin commissioner—

Chairman DUFFY. But "depends" doesn't work well. There is no specificity in who is on the joint committee. I don't even know. It is not in here. Again, it goes to the point of the first question, you are referring me to the joint committee, and when I talk about the joint committee, we don't even know who is going to represent us.

And again, I just would ask you to—and maybe as we talk about this today, that is maybe a point of agreement that, again, I think there has been unanimous agreement that if the deal was still to go through, clarification would be still really important.

So my time is long expired. I now recognize the gentleman from Missouri, Mr. Cleaver, for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman.

Mr. Nickel, are you aware that the covered agreement also has to go before not only this committee, House Financial Services, but also the House Ways and Means Committee, and the Senate Banking Committee?

Mr. NICKEL. I was not aware of that, but I would look forward to the opportunity to be there myself or have someone else present in front of those two bodies.

Mr. CLEAVER. So you would agree, I think, that this is not something that is being rushed through and that we are not giving optimum participation to interested and impacted parties?

Mr. NICKEL. Absolutely, Congressman Cleaver. I think it is a great opportunity. But what we struggle with is the fact that the language itself—there doesn't seem to be any authority to do anything about it. It is a holdover. It has allowed for review by these three pertinent committees, but not to be vetoed or changed, et cetera.

Mr. CLEAVER. Right, right. Now, do you know any trade agreement where States are involved?

Mr. NICKEL. Sir, that is not in my wheelhouse. I don't spend my time on trade. I work to support State insurance regulation.

Mr. CLEAVER. I think it would be defined as a trade agreement, don't you agree?

Mr. NICKEL. I wish it was a trade agreement which would have a lot more clarity and participation on the behalf of interested parties and all—

Mr. CLEAVER. I know, but a trade agreement doesn't mean that—if we define a trade agreement only by what we are able to—how we are able to influence it, that is kind of a weak definition. The point is, my question was going to be—and you answered it—and that is that some of your recommendations did, in fact, find their way into the agreement, right?

Mr. NICKEL. That is correct, sir.

Mr. CLEAVER. And nobody should expect everything they want into everything, is that right?

Mr. NICKEL. That is correct, sir.

Mr. CLEAVER. Okay, now, thank you. We have over 7,000 insurers in the United States. And all of them are controlled by the State in which they are domiciled. And so this is a unique system. And you said—I don't know if you are minimizing it—a small group of States were participants.

Ms. Pusey, can you talk about transparency in this whole process?

Ms. PUSEY. I think we are probably in the camp that the chairman was referencing, that while we were enthusiastic and supportive of the results of this, I think the process could clearly have been improved from what we understand. So how do you oppose transparency? I think making all efforts, at the same time recognizing I think that there will be some restraints on that.

States are not constitutionally recognized to be able to negotiate international deals. That is why—that was a lot of the impetus, as you also referenced, Congressman, for why we created the Federal Insurance Office with this very, very limited authority. It has no regulatory authority, but it has limited authority on international agreements.

So while I think we would all embrace more transparency, nothing is ever wrong with a little more clarity, there is a limitation I think constitutionally with just how much the States could be involved in an international agreement. And that is where I think we all argue that there should be a consultative role, which it sounds like there was some of that.

Mr. CLEAVER. Mr. McRaith, if you would speak to the issue of stakeholder involvement?

Mr. MCRAITH. We asked the State regulators in an unprecedented, unprecedented in any—State regulators are not involved in any trade agreement delegation, not involved ever before in any international agreement in a negotiation delegation, never before we asked the State regulators to create a small task force—we didn't tell them how many, we didn't tell them whom—those State regulators were invited to and did participate in every negotiating session.

We briefed them before and after every negotiating session. We shared with them documents before they went to the E.U. We received their input on those documents before they went to the E.U. During the negotiating sessions, they were asked for technical insight and input. They provided it at the table, not in the room, at the table as a member of the U.S. delegation.

So we received State regulator impact. We worked with this committee. The other three committees of jurisdiction spoke with them before and after every negotiating session multiple times in recent months. We worked with all of our stakeholders, particularly those engaged in the E.U. and the U.S. Not all of Mr. Chamness's companies, but those that operate in the E.U. and the U.S. and have a stake in the outcome of this agreement.

And we worked with the entire Executive Branch of the Federal Government to get a deal to this committee and the other three committees that puts America first.

Mr. CLEAVER. Thank you.

Chairman DUFFY. The gentleman's time has expired. The Chair now recognizes the vice chairman of this subcommittee, the gentleman from Florida, Mr. Ross, for 5 minutes.

Mr. ROSS. Thank you, Mr. Chairman. And I thank the panel for being here. My first impression has to do with process. And that is what concerns me, because this isn't a trade agreement. If it was a trade agreement, we would have an up-or-down vote. And we have the opportunity to review for 90 days, but really what can we do as a Congress? This is going to be left up to the Administration, to the Treasury Secretary. And so that concerns me from one aspect that will stay over there.

My other concern is, as I mentioned in my opening statement, what benefit do we have for the consumer, for the policyholders? And I know that it was said that we will have the benefit of the consumer protections that are so good under the State regulation system.

My question to the panel is, what other benefits do the consumers or the policyholders anticipate from the implementation of this agreement? And specifically, is there a benefit in the rate-making process that will inure to the benefit of the consumer? In other words, will they have a better rate as a result of this?

And, Commissioner, I will start with you.

Mr. NICKEL. Thank you, Congressman. Our concern with the elimination of collateral for European reinsurers is the fact that we now, as U.S. regulators, are going to have to figure out a new mechanism by which to assess that risk which has now been transferred to more of us—

Mr. ROSS. Will you put it in the guarantee fund? Will you require more assessment in the guarantee fund? Or how will you balance that? And is it going to impact the rate?

Mr. NICKEL. Correct. Hopefully, nothing will end up in the guarantee fund as a result of this. But what I would say is, as regulators, now that there is no collateral, and there are words on a paper now that insurance regulators are going to have to trust from E.U. reinsurers as to their financial strength, no more collateral here, $30 billion will be going out the door, that the U.S. insurers are going to have to work now with ceding companies to manage that risk, possibly employing other financial strength indicators or capital requirements which will ultimately raise rates that your constituents will pay.

Mr. ROSS. Mr. McRaith, as a former insurance commissioner, how do you respond to that?

Mr. MCRAITH. Two pieces. Let's be factual about reinsurance collateral relief. The States adopted it as an accreditation standard effective in 2019, meaning every State would have to adopt collateral reform. Of the States that have adopted it, 31 companies have received relief. Thirty of those companies are now posting 10 percent or 20 percent of the collateral they posted a few years ago. So the notion that we are going from 100 to zero is complete fiction.

Second, that cost savings gets passed on to our primary insurers. But third, and more importantly, our flagship companies operating in the U.S. and the E.U. will not have to post billions of dollars in Europe in compliance costs that otherwise can be used to support affordable, accessible insurance products in the United States.

Mr. ROSS. Ms. Pusey, the impact of reduced or no collateral at all being held, does that increase reinsurance capacity? Or how does—

Ms. PUSEY. We would hope it would be filled up and down the chain, yes. We think you are going to have more creativity, more products available, and clearly I think one could expect some impact to the rating side.

If I could, Mr. Ross, I just wanted to come back to a comment made about the quality in some of the perception that the consumers are exposed because some of the rules won't be carried forward. As we understand it, they are quite robust, because they do take quite literally from the current NAIC model. So there will be a capital surplus requirement on these insurers from Europe, a consent to jurisdiction in our courts, a consent to a service of process, 100 percent collateral if they resist timely payments.

And I have four or five others. The point is, it does carry forward a lot of those protections. So we would certainly hope that this would not threaten and, to the contrary, would actually enhance the U.S. policyholders' experience with insurance, both in terms of product and price.

Mr. ROSS. And, Mr. Chamness, if I might, because I am running out of time here, how do we unscramble the egg? Let's assume the covered agreement goes through. Let's assume that 2 years from now, as we get close to permanency in the 5 years, it is not what we thought it would be. How do we get out of it? Or can we get out of it? And what impact will that be?

Mr. CHAMNESS. I think the greater concern is the covered agreement obligates the State regulatory system to take certain steps. And if those steps aren't taken, I think it comes apart on its own. So I think there is significant concern over that.

Also, I would point out—and to your earlier statement, and it was a discussion just previously about why were State regulators in the room, are they with any other trade agreement, this is a very particular type of trade agreement. It has no oversight in terms of State regulators, State legislators, or Congress, in terms of an up-or-down vote. It is simply a 90-day layover period. And it is binding and it preempts State law.

So I think having State regulators in the room for this type of agreement is a very prudent measure.

Mr. ROSS. Thank you, and I yield back.

Chairman DUFFY. The gentleman's time has expired. The Chair now recognizes the gentlelady from New York, Ms. Velazquez, for 5 minutes.

Ms. VELAZQUEZ. Thank you, Mr. Chairman. Ms. Pusey, many observers note that this agreement is vital because of its commercial significance and for the level playing conditions it creates. At the same time, others note a less tangible, but equally important outcome. This is the first time the E.U. has taken such significant steps to recognize the U.S. State-based insurance regulatory framework.

Can you talk about that?

Ms. PUSEY. As I said in my testimony, I agree with you. I think it is a historic recognition. We have never had an agreement where the second-largest market to the U.S. would actually say, we recognize your State-based system.

And the implications are pretty important. They are not just important today for relieving this pressure that is on our companies doing business there, because as we said, it is going to prevent them from imposing this upstreaming, if you will, of Solvency II, which no one in the U.S., regulators or industry, ever advocated for here.

So it is helpful in that sense. But we also think it is important because it is going to, I think, increase the leverage that the U.S. has at the international negotiating table. We have talked, I think, before this committee about Team USA, which is a collaborative effort between the FIO, the Federal Reserve, and our NAIC, and at the international table dealing with issues on ComFrame, which is a common framework for internationally active insurance groups. And within the ComFrame is a discussion about an insurance capital standard, which is again a global capital standard.

For the U.S. to be at that table empowered by European recognition of our system, we ought to be pretty forceful at pushing back. So we have been good at pushing back. This is further ammunition. So to your point, I think it is incredibly valuable, not only historic, but valuable.

Ms. VELAZQUEZ. And can you please comment on specific commercial or supervisory barriers that this agreement will eliminate?

Ms. PUSEY. Specifically, we have companies that are U.S.-based and they are doing business through a subsidiary or branch in the European Union, and about a year ago, what we started to feel—this is different from the reinsurer issue, which has been ongoing, but in the primary space, regulators in Europe were telling our companies we don't recognize your home jurisdiction is equivalent to Solvency II in Europe, and therefore we are going to require you to hold more capital, consistent with their rules under Solvency II. We are going to require you to do an E.U. ORSA, which is a self-assessment that companies have to do, and comply with corporate governance rules.

We even had companies talking about threats to executive compensation being sort of snatched back because the European governance rules are different than the U.S. governance rules. So those are some of the specific ways in which we were feeling threatened, if not outright discriminated against, under the situation if it is not cured by this.

Ms. VELAZQUEZ. Thank you. Mr. McRaith, the joint committee established by the agreement is an interesting concept that is used quite frequently in trade agreements, and we have alluded to that. Do you support NAIC and State regulator involvement in that joint committee? And how do you see the joint committee strengthening the relationship between the U.S. and Europe on insurance issues?

Mr. MCRAITH. As mentioned earlier, we did not build out all the details of the joint committee in the agreement itself. That would have required potentially 40 or 50 more pages to identify what is a quorum and what is the membership, all of these kinds of details you are familiar with for committee construction.

Absolutely, a State regulator should be on the joint committee, particularly the State regulator whose company might be affected or who would be the thought leader on the issue that is being discussed. What the joint committee is intended to do and the purpose—the role it will provide in relation to the broader agreement is to allow for collaboration and cooperation, because both the E.U. and the U.S. receive benefits from this agreement, important benefits for our consumers and our industry, and both sides want to see it work. The joint committee will foster that collaboration, which will be so important in the coming years.

Ms. VELAZQUEZ. Thank you. Ms. Pusey, would you like to comment on that?

Ms. PUSEY. No, we would be in agreement that we have to have robust participation by the NAIC on this joint committee. We think it will further enhance the relationship with the European Union. We fully expect that they will be consulting with the European Insurance and Occupational Pensions Authority (EIOPA), which is their sort of parallel to—in many ways, not exactly, but in many ways parallel to our State regulatory system, because you are going to want that expertise in the room to deal with those unique issues that will come up.

Ms. VELAZQUEZ. Thank you. I yield back, Mr. Chairman.

Chairman DUFFY. The gentlelady yields back. The Chair now recognizes Mr. Pearce from New Mexico for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman. I appreciate each one of the witnesses being here today.

Mr. Nickel, you just heard Ms. Pusey say that Solvency II is going to completely recognize the State-based system. Do you find that to be an accurate assessment?

Mr. NICKEL. I wish that were true, Congressman, but I think it is the other way around. I think the Europeans are trying to impose the Solvency II model on the United States, and this is one avenue to do that. We are very concerned about that piece, as well as the language in the covered agreement itself, which ultimately preempts what we have been trying to do with regards to collateral reduction, the fine work we have been doing on collateral reduction.

It takes all the work that we have been doing and then forces us to map over an agreement that was put together—

Mr. PEARCE. Sure, I need to move on, but tell me a little bit more deeply about the impact on consumers of the collateral changes that you are saying need to be implemented. Tell us more at the individual policyholder level what that means?

Mr. NICKEL. Sure. First and foremost, ultimately the collateral that is posted to recognize the risk taken is the ultimate safety net for consumers.

Mr. PEARCE. I understand. But what's the difference between the U.S. and the European markets?

Mr. NICKEL. The U.S. market requires collateral on behalf of foreign reinsurers, because of the fact that we are not comfortable with—

Mr. PEARCE. At a greater level?

Mr. NICKEL. Sorry?

Mr. PEARCE. At a greater level?

Mr. NICKEL. Yes.

Mr. PEARCE. Providing greater security?

Mr. NICKEL. Right, because our U.S. reinsurers—

Mr. PEARCE. No, that is all I need, just more security.

Mr. NICKEL. Yes, sir.

Mr. PEARCE. Mr. Chamness, describe the size of your members basically as operations. Are they large, small? You have those member associations, and the Europeans want to come and sell in our market, and they want to bring their rules over here more or less. Is that correct?

Mr. CHAMNESS. Correct.

Mr. PEARCE. They don't want to have to piddle around with all the States. That is a little bit beneath us here. We don't want to mess with you State regulators. And so we want a nice—we want to clear the playing field out for us, so compare the size of your members with the Europeans that want to come here.

Mr. CHAMNESS. Our members, on a consolidated basis, write $230 billion of premium. They range from very large, including international, to regionals, one State writers, and small rural mutual that write in rural America.

Mr. PEARCE. What percent are State and what percent are the small guys?

Mr. CHAMNESS. What percent are the small guys?

Mr. PEARCE. Roughly, just a lot or a small group or—

Mr. CHAMNESS. Of the 1,400, probably 600 are small guys—

Mr. PEARCE. Almost half. Almost half just mom-and-pop operations out there writing insurance, trying to make it work for their neighbors.

Mr. CHAMNESS. Correct.

Mr. PEARCE. Mr. McRaith described—I guess he was describing your positions as theatrical and conjured fiction. Mr. Nickel and Mr. Chamness, do you have any response to that? It seemed like a fairly—

Mr. CHAMNESS. Let me just start where you began, and that is, I don't think it is theatrical. When we have read this agreement and we know that the primary objective the U.S. had going into the negotiations was to obtain equivalence, which has a very specific meaning for the European Union, and the word does not appear in the document. And mutual recognition, other proxies for that also are not in the document. So we have concerns about that and we have concerns about the permanence of the treatment that our U.S. insurers doing business over there will receive.

Mr. PEARCE. Yes. So, again, trying to get this whole playing field underneath us, Europeans want to come here and use their rules to sell to our market. We would like some access to their market and we would like them to recognize our system. Is that basically the dispute, the totality of the dispute? Is it close enough, Mr. Nickel?

Mr. NICKEL. That is pretty close.

Mr. PEARCE. Okay, so—and you are concerned because you feel like the American consumer might be disadvantaged? We see that the operations coming in here are going to be the big multinationals, not going to be mom-and-pops come here. Your mom-and-pops are not going to go over there and sell insurance, are they?

Mr. NICKEL. No, they are not.

Mr. PEARCE. They are probably going to stay in their neighborhoods.

Mr. NICKEL. Correct.

Mr. PEARCE. So all I do is think in my simplistic way back to my first days in owning a small fishing and rental tool company in Hobbs, New Mexico, just working in that neighborhood oil fields, wanted to buy the best insurance possible, so we went out—and I didn't know anything about insurance, but Lloyd's of London sounded very big, so we bought that insurance from them.

And we had our first claim. This was a claim, a moderate claim, $50,000 to $100,000. Lloyd's of London told us we are bankrupt, we are not going to pay. So we want to let people from over there that we can't have any responsibility, we can't touch them, they are going to come in here with their capital requirements and tell us they can't pay. Mr. McRaith tells me that is a good deal and it is theatrical for me to believe differently. Maybe it is.

I yield back.

Chairman DUFFY. The gentleman's time has expired. The Chair now recognizes the gentleman from Nevada, Mr. Kihuen, for 5 minutes.

Mr. KIHUEN. Thank you, Mr. Chairman.

I just have a couple of very quick questions. Thank you all for your presentations this morning. Mr. McRaith, can you please provide some more detailed thoughts on how this covered agreement will impact consumer protections, particularly for constituents of mine in the State of Nevada?

Mr. MCRAITH. Sure. First, as I mentioned earlier, the covered agreement will improve the affordability and availability of insurance products in the United States. Some of our flagship companies that operate in the U.S. and the E.U. would have to post billions of dollars potentially in compliance costs that can otherwise be used in the U.S. to invest in new products and keep their rates affordable.

Second, the decrease in reinsurance costs will help those consumers, particularly in areas affected by natural catastrophes, so that their primary insurance products are more likely to be affordable.

Third, the agreement preserves and enhances essential consumer protections so if there is a reinsurer from the E.U. who is not paying claims, that reinsurer immediately can be required to post additional collateral to protect the ceding insurers and consumers.

And then finally, I would say it is—this is not a binary choice between industry and consumers. This agreement has the benefit of benefiting industry and those benefits will also benefit consumers. So in its totality, this is an agreement that serves all of the U.S. industry interests and U.S. consumer interests.

Mr. KIHUEN. Thank you. And just one more question. I know there have been some complaints that this could be a backdoor for the E.U. to impose their standards on U.S. insurers. We also need to recognize that we are living in an increasingly interconnected world where the barriers for U.S. companies to enter foreign markets are becoming smaller and smaller. Can you speak on how you think the U.S. can adequately achieve balance between lowering the barriers for insurers to operate internationally while at the same time making sure that one country can't single-handedly change regulatory standard globally?

Mr. MCRAITH. First of all, what the agreement does is endorse, embrace, enshrine our U.S. system of supervision at the State level for the first time in history in an international agreement. The agreement does not call for the States to do anything other than what they are doing already.

Second, the E.U., as a consolidated market, is actually larger than the U.S. market. So we need to preserve opportunities for our companies to operate there, to compete there.

And then, third, what is even more important is that our companies need certainty about how the E.U. and the U.S. are going to work together so they can compete in those massive developing economies like China, India, Brazil, and Indonesia, they can use that capital they have accumulated and invest in organic growth in developing economies around the world.

Mr. KIHUEN. Thank you, Mr. Chairman.

Chairman DUFFY. The gentleman yields back. The Chair now recognizes the gentleman from Florida, Mr. Posey, for 5 minutes.

Mr. POSEY. Thank you, Mr. Chairman. Mr. Chamness, outside the reinsurance collateral issues, I have heard concerns that the U.S., under this covered agreement, will be required to make significant changes to our State system of regulatory supervision, which as you know is based on legal entity supervision.

Article 4H of the agreement requires the U.S. to create a group capital requirement which from my understanding differs from the current State regulation in two ways. One, it requires that the States adopt a group capital assessment, which we don't have today. It also requires a lead State regulator to have the authority to act, including by requiring additional capital, if it sees an issue as a result of the group capital assessment.

How do you view the capital requirements in article 4H? Could the corrective preventive measures included in the agreement require, for instance, increases in capital, capital movement between affiliates, or other fungibility mandates that go against the United States-based system of insurance solvency?

Mr. CHAMNESS. Thank you for the question. I think you have summed up the elements of article H that concern us very well. The Europeans have a different way of regulating. We focus on legal entities and we focus on solvency for those legal entities. They focus on group capital and group supervision. And it is different.

And to the extent that this agreement moves us further in the direction of European standards, where we would be forced to change the way we regulate here in the U.S. and to really take away the focus that we have in the U.S., which was one of our great benefits, is we focus on the policyholder. In Europe, they have much greater emphasis on creditors, on investors, and preserving the insurance company.

In the U.S., we let insurance companies fail where they deserve to fail, and first we try to rehabilitate them. Then, they may fail. And we also have a guarantee fund system here, which is different than Europe. They don't have a similar structure to deal with insolvencies and to pay claims after insolvencies, claims that are actually paid for by the remaining companies in the market.

So it is a much different system. And as we look at the authority to preempt State law contained in this agreement, the permanent committee moving forward that will further fine-tune the agreement and perhaps commit us to future other changes to our structure, we are very concerned that we will be implementing more European regulatory law into the U.S. system.

Mr. POSEY. Yes, I am afraid any time we talk about giving up sovereignty, a mini-U.N. where we carry the burden and everybody votes against us every opportunity they have. But a follow-up, last Congress, we passed legislation into law to ensure that the regulator of a savings and loan holding company cannot raid the assets of an insurance company subsidy in order to prop up a failing subsidy affiliated with the overall holding company.

This walling off of insurance, if you will, is to me one of the strengths of the way that we regulate our system, and it is because it places the emphasis on the policyholders. In other words, we are protecting the policyholders, first, over failing institutions, and second, which you just mentioned is different than the way they do it in Europe. I have always considered this to be one of the benefits to the legal entity regulation in the United States, and I wonder if we move toward the group supervision provisions, if it will alter our system? I clearly believe it will. But my question to you is, do you think the priority will still be protecting the policyholders?

Mr. CHAMNESS. Again, I think if we adopt more European-style regulation, it won't. And I think your example of the law to basically wall off the insurance legal entity from the insured depository institution that may be part of an insurance group is a very apt comparison to the type of challenges we are concerned about under this agreement if more European regulation comes here.

Mr. POSEY. Mr. Chairman, I see my time is about out. I yield back.

Chairman DUFFY. The gentleman yields back. The Chair now recognizes the gentlelady from Ohio, Mrs. Beatty, for 5 minutes.

Mrs. BEATTY. Thank you so much, Mr. Chairman, and Ranking Member Cleaver. And let me also thank all of the witnesses who are here today.

My first question goes to you, Mr. Chamness. In your testimony, you stated that the U.S. Trade Representative and the Federal Insurance Office conducted the covered agreement negotiating meetings in a closed, confidential manner and failed in their commitment to meaningfully include State regulators in the negotiating process. I think you went on to say that State regulators were mere observers in the negotiating process.

I then heard Mr. McRaith in his oral testimony, I think, mentioning that Ranking Member Cleaver outlined a whole litany of inclusive things when he laid out the steps that the FIO and the USTR. took to include State regulators and to be transparent in the process.

With all of that said, I won't go through all of the things that have already been outlined, but I guess, after hearing that compelling argument, it appears that the USTR and the Federal Insurance folks went far beyond the call in engaging the stakeholders, my question to you is, what about that process do you find lacked transparency or didn't adequately involve the State regulators?

Mr. CHAMNESS. Thank you for the question. We have two participants here at the table, so perhaps my characterization of the way State regulators were included in the negotiations could be amplified by either participant.

But I think we just heard Leigh Ann say that the process could have been improved. And it was a situation where having an agreement that has the authority to preempt State insurance law, automatic authority with no oversight or up-or-down vote either by legislators at the State or Federal level, there was very much a meaningful role there for State insurance regulators to play.

Whether they did effectively in these negotiations, and whether Commissioner Nickel can talk about his participation in any greater detail than he did earlier, I guess I would ask him or ask former Director McRaith to describe the participation further.

Mrs. BEATTY. I will give you a few seconds, too. I just thought—I understand what you are saying, it could have been better. But I guess to be helpful to me, and you are an expert here, what would be the, "could be better?"

Mr. CHAMNESS. I think that having State regulators negotiate the agreement in conference with FIO, working side-by-side in a transparent way, and frankly including more elected leaders like yourselves in the process, at least to review and approve the agreement that has been reached before it goes into effect and preempts State insurance law, bypassing the legislative process.

Mrs. BEATTY. And when you say "yourselves," I'm assuming that means Congress, as I heard in this testimony that we already have in place where you can consult with Congress either in person or by telephone, before negotiations begin, before and after each session, and before the negotiations were finalized, is that not enough? Is there more that we should be doing? Because it said in person or in telephone with us.

Mr. CHAMNESS. I think the process was the process and the agreement is the agreement. And as we talk about and have presented our comments on the agreement, it was consultation with the U.S. Treasury and the USTR informing Congress about their objectives here, and I read from their objectives. One was to obtain treatment of the U.S. insurance regulatory system by the E.U. as "equivalent" to allow for a level playing field for U.S. insurers and reinsurers operating in the E.U.

Regardless of the process, though I do care about the process and I think the question is an excellent one, perhaps for future use as we consider how to do a different covered agreement, but on the terms of the agreement that have been released now and that we are talking about today, we don't believe it met the objective that the U.S. itself, the Treasury and the USTR, set forth in terms of our U.S. objective in the agreement.

Mrs. BEATTY. Okay.

Mr. NICKEL. Congresswoman, may I just chime in for 2 seconds? I appreciate it. Thank you. I would just add, in terms of revising the process, insurance matters are very technical in nature. They touch each company in different ways. Having an avenue for participation by those key stakeholders, as well as our consumer representatives who would have input there, would have been very helpful along the way.

Having the ability for me to consult with my own staff; for the insurance regulators themselves to bring in the rest of their group to get consensus might have driven outcomes, which may not have put us at this table today in opposition. Thank you.

Mrs. BEATTY. Thank you. I yield back.

Chairman DUFFY. The gentlelady yields back. The Chair now recognizes the former Chair of this subcommittee, who is the current Chair of the Financial Institutions Subcommittee, the gentleman from Missouri, Mr. Luetkemeyer, for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman, and you are doing a great job today. Thank you very much for the opportunity to be here.

Also, thank you for the hearing. I think it is vitally important that we have this hearing today. I think part of our duty as I have said many times is not just legislative, it is oversight, to provide oversight and direction. In this situation, we are providing oversight over the FIO Director and his activities. And I think it is important that we help him, that we guide him, and provide him the leverage that we need to do to help him do his job. And I hope that he comments on that. I think that is what our objective was for the last 2 years: to be able to give him the tools and leverage to get his job done.

But before I do that, I will make a couple of comments. I think today we have an example of the problem we have in the insurance industry. We have two groups representing two groups of insurance companies that disagree. Imagine that.

And then we have a regulator who had 5 years to come up with a solution for this problem and did nothing. And now, we are nipping at the heels of the agreement that we have, and we have dumped this whole problem in the Director's lap. And he has to deal with a dysfunctional group of industry folks and a regulator who doesn't want to get along and do anything, and he has to come up with an agreement to make this all work. I take my hat off to you, Mr. McRaith. You have done a great job. Is it a perfect agreement? Probably not. Could it be tweaked? Probably.

But I think if the industry is serious about getting something done, I will tell you from my perspective they better get on the same page, because I am up to here with this dysfunctional infighting with the industry and the regulators and nobody getting anything done. You are going to go backwards as an industry if you don't get together. That is my comment.

Now, Mr. McRaith, I have had a couple of companies in my district and my State who have been directly impacted by the request from Ireland, Belgium, and Germany to have a physical presence over there. So this is a big deal to me. I think that you have done a good job in negotiating, trying to thread the needle.

One of the comments that has been made that concerns me is regarding "equivalency." We have heard that term thrown around a couple of times, both from Mr. Nickel and Mr. Chamness. Would you please address what you believe is the solution to this or the addressing of this issue and the like?

Mr. MCRAITH. Yes. Thank you, Mr. Chairman. First of all, we sent that letter in November 2015 at the commencement of the negotiations using the word "equivalence." As we did that, we learned what I alluded to earlier, which is that every time you talk to a lawyer or a so-called Solvency II expert, you get a different explanation about what "equivalence" actually means. So we were focused on the outcome.

We changed our focus. Let's have in the agreement clarity about how U.S. companies will be treated when they operate in the E.U. We don't want equivalence. And that is because an equivalent country like Switzerland has a global group capital requirement, global group reporting and governance, exactly what we don't want.

So paragraph 4H, as discussed by Mr. Posey, and I regret that he is not here to hear this, because he misunderstood it, what that paragraph says is the United States will supervise its companies however it deems appropriate. The States have said for 2 years now we are going to develop a group capital calculation, and what that paragraph 4H says is, as the States do that over the next 5 years, U.S. companies operating in the E.U. will not have to be subject to Solvency II compliance burdens, including potentially billions of dollars in additional capital.

So the notion of equivalence we surpassed because our companies are being treated entirely fairly with—and being able to supervise as the States deem appropriate without global group capital requirements, global group governance and reporting.

Mr. LUETKEMEYER. Thank you. One more question for you, quickly. One of the things that we did in a hearing last fall was we had a hearing similar to this and discussing this issue, and we made the comment during that, that if the Europeans wanted to penalize and punish our companies, there could be retribution against them in this country if they are going to play that game. Does this agreement affect us in any way so that we can't—it ties our hands so that we can't be able to have retribution or are penalized in any way these companies that try to come here and push their stuff on us?

Mr. MCRAITH. Mr. Chairman, first of all, I want to thank you for the letter that you provided November 29th, I think of 2016, and frankly, although our exchanges were not always pleasant, you were extremely forceful about the importance of representing U.S. interests.

What this agreement does is allow the U.S. companies to be supervised in the U.S. as the U.S. determines appropriate. There are no penalties for that. If, however, U.S. companies in the E.U. are not supervised according to this agreement, then the reinsurance reforms that will benefit E.U. reinsurers can be retracted. And then vice versa. If the U.S. doesn't perform on the reinsurance provisions, which, by the way, the States have adopted as an accreditation standard, then our companies in the E.U. can be treated adversely.

Chairman DUFFY. The gentleman's time has expired.

Mr. LUETKEMEYER. Thank you.

Chairman DUFFY. The Chair now recognizes the gentleman from Massachusetts, Mr. Lynch, for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman. And I want to thank the witnesses for their help.

I am very suspect of these international negotiation agreements that exclude Congress and exclude the State regulators in this case to a certain degree. I have a healthy distrust of what the U.S. Trade Representative has been doing in the past.

I was an iron worker for about 20 years, and I used to work at the General Motors plant in Framingham, Massachusetts. Then they negotiated NAFTA, and a bunch of plants, including the one I had worked at, closed down and moved over the border.

So I have real distrust about allowing industry to negotiate—the people with the direct financial interest to negotiate these agreements outside of the purview of Congress and outside the representation of the people who elected us. I have a real mistrust about that.

We negotiated a trade agreement with South Korea. It included automobiles. I go to South Korea. I spent 3 or 4 days there. Major, major country. Big superhighways. I saw two U.S. cars, two. One was the one I was riding in from the embassy. The other one was my security detail right behind me. That was it.

I went to Japan. We have a big trade agreement with Japan. I couldn't find an American car. If you go outside this building, you can't spit without hitting a Japanese or a South Korean car.

So when we sit down in negotiations and want equivalency, that was the goal of our agreement, our insurance agreement, was to get equivalency for our system. And then I pick up the agreement and the word "equivalency" does not appear. It does not appear. We negotiated this agreement. It does not mention equivalency that U.S. standards will be recognized and acknowledged and given full force and effect in the E.U.

So as far as I am concerned, based on reading the agreement, and I know there is a lot of goodwill out there and let's all play nice, it doesn't give us what we were looking for. It doesn't give us equivalency in the E.U. It gives us the hope that maybe in the future we could get that, but we don't get it.

And what's more, it allows for the States' laws to be preempted. And that—I think one of the great things about our State-driven insurance regime, our system, is that it is very close to the people. And it requires support at the State level. And that is where I think the public's influence is the strongest and the big industry people's influence is the weakest. It is a good match.

And I just have great, great trepidation about this whole—I am a new member of this committee. I have only been here for 2 weeks. But I just have great misgivings about how we did this. I would like Congress to be part of this process. I really would. I hate this. You go negotiate the agreement, and when we find out at the end what it has in it, and you surprise us, and then we have an up-or-down vote. Or in this case, it is just a 90-day layover period; we don't even get a vote. Congress negotiates war and peace, life and death, every major issue in our society. But when it comes to trade agreements or international insurance agreements, we are excluded from the process.

So I would like a process that allows the people—I have 727,514 people that I represent in Boston, Quincy, Brockton, and a bunch of towns in Massachusetts. I would like my people—my people through me—to have some input into this process. And when I feel confident that their interests have been acknowledged and been included, then I will vote for this, then I will support it. I don't like the process. There is a lack of transparency here. And we have to change the system, the way this all works.

I appreciate all the really smart people in the insurance industry, but having the people with the most direct financial interest, their own financial interest at the table negotiating this while the people who are going to be affected by it are outside the process is not right. It is just not right. And this system was created a long time before I got here, but I think we ought to have a bipartisan agreement that the people we represent should be part of this process at some point.

So with that, Mr. Chairman, I yield back the balance of my time.

Chairman DUFFY. The gentleman yields back. The Chair now recognizes the Vice Chair of the Financial Institutions Subcommittee, the gentleman from Pennsylvania, Mr. Rothfus, for 5 minutes.

Mr. ROTHFUS. Thanks, Mr. Chairman. I want to follow up on Mr. Lynch here, because this is one of the issues I was struggling with last night. I read my Constitution. Article I, Section 8 provides that Congress shall have the power to regulate commerce with foreign nations and among the several States and with Indian tribes. Does this covered agreement regulate commerce with foreign nations, Mr. Nickel?

Mr. NICKEL. I believe so.

Mr. ROTHFUS. Mr. Chamness?

Mr. CHAMNESS. Yes.

Mr. ROTHFUS. Ms. Pusey?

Ms. PUSEY. Yes.

Mr. ROTHFUS. Mr. McRaith?

Mr. MCRAITH. This agreement does not regulate anything. It is an agreement between countries about how they will separately regulate and deal with the industries operating within their territory.

Mr. ROTHFUS. You don't think this regulates commerce? Is it a trade—

Mr. MCRAITH. This is a regulatory agreement that articulates how the U.S. will regulate U.S. industry and the E.U. will regulate E.U. industry.

Mr. ROTHFUS. Is it a trade agreement?

Mr. MCRAITH. It is not a trade agreement.

Mr. ROTHFUS. I thought I saw—some of you were mentioning this being a trade agreement.

Mr. MCRAITH. I have heard that. I have never said that. In fact, I have said the opposite. It is a covered agreement. If it were a trade agreement, it would be called a trade agreement. A covered agreement refers to prudential insurance and reinsurance matters.

Mr. ROTHFUS. Dodd-Frank requires consultation with Congress on covered agreements. Does consultation equate the power to regulate? Again, this is a threshold issue that I was kind of struggling with last night as I look at this covered agreement, trying to figure out, where does Congress gets its say?

Because I think this does regulate commerce with foreign nations, which begs the question, where is Congress' power to regulate? Us having a 90-day consultation period, us not having an opportunity to have an up-or-down vote on this, compare this with what we did with trade promotion authority. We have Dodd-Frank. We said the Secretary of the Treasury and the United States Trade Representative are authorized jointly to negotiate and enter covered agreements on behalf of the United States.

Looking at TPA, and it says that the President and the USTR can enter an agreement. But then it is up to Congress to ratify that. And that is where we get to exercise our constitutional power to regulate commerce.

We have already seen parts of Dodd-Frank, or at least one part of Dodd-Frank, that has been challenged constitutionally, and it is currently held up in court. That is with the structure of the CFPB. And I guess I am just struggling with that.

Where do the people that we represent, the total notion of self-rule and self-government—we have been talking about this for years on our side of the aisle, the opportunity for us to be the voice of the people.

The Congress is where government of the people, by the people, for the people happens. And here we have a covered agreement that will regulate commerce among the nations, and we are not getting a say. We just get to consult.

Mr. McRaith, one of the many things that stands out to me about this covered agreement is the date it was sealed, 1 week before the inauguration of a new President. As you know, President Trump made negotiating better deals a hallmark of his campaign. He has argued that the U.S. has not made deals with other countries that provide the most benefit possible for American workers and firms.

Since the covered agreement was reached before the new President could come into office and leave his mark on these negotiations, I am curious about the extent to which negotiators consulted with the transition team before the election. Were there such any consultations with the transition team?

Mr. MCRAITH. These agreements were conducted confidentially with the input of the entire delegation after extensive consultations—

Mr. ROTHFUS. Okay, so the question was, was there consultation with the transition team, yes or no?

Mr. MCRAITH. The transition team was not part of our confidential U.S. delegation.

Mr. ROTHFUS. Okay. Why was the covered agreement reached on January 13th? Any significance to that date?

Mr. MCRAITH. First of all, our industry, U.S. reinsurers were losing opportunities every day. Our primary insurers were confronting potentially billions of dollars in compliance costs on an urgent basis.

Mr. ROTHFUS. Was January 20th at all a figure? Was January 20th a consideration?

Mr. MCRAITH. No. So we provided to you on January 13th—because it needed to be provided on a day that both Chambers of Congress were in session, so I suppose theoretically we could have provided it the morning of the 20th, but I think our perspective was to get it to you as soon as we finished it, which was that day.

Mr. ROTHFUS. Last question. I just want to go back to the earlier issue. Have any of you ever considered the constitutionality, or have your groups considered the constitutionality, of this covered agreement? Yes or no?

Mr. CHAMNESS. No.

Mr. ROTHFUS. Has that been studied?

Mr. CHAMNESS. Not by us.

Mr. ROTHFUS. Mr. McRaith?

Mr. MCRAITH. I am not a constitutional lawyer, Congressman, but the question is, can we reach an agreement that serves the best interests of the United States? And that is what we did.

Mr. ROTHFUS. I yield back. Thank you.

Chairman DUFFY. The gentleman's time has expired. The Chair now recognizes the gentleman from California, Mr. Sherman, for 5 minutes.

Mr. SHERMAN. In Washington, there are lies, there are fibs, and there is misuse of the word "consultation." All too often, consultation means you go to a few leaders in Congress, you say here is what we are doing, but we don't care what you think, we will pretend to care what you think, we won't tell anybody else in Congress what you are doing, and we will call that a "consultation." And that somehow makes us a democracy, though I haven't figured out how.

Speaking of consultation, to what degree were the 50 U.S. insurance regulators at the State level involved in this process, Mr. McRaith?

Mr. MCRAITH. Sir, Congressman, as I mentioned before your arrival, in a completely unprecedented manner, we established a mechanism to include the State regulators as part of the negotiating delegation. So we asked—

Mr. SHERMAN. Is this agreement—

Mr. MCRAITH. —them to form a small team, which they did—

Mr. SHERMAN. —binding on—

Mr. MCRAITH. They were part of every step of the negotiations.

Mr. SHERMAN. Thank you. I hear you. I am going on to another question. Is this agreement binding on them? And on the—do they have to comply with it in how they regulate insurance companies around this country?

Mr. MCRAITH. In fact, the provisions regarding group supervision are already what the States do or what they have committed to do and it gives them 5 years to do it. In terms of reinsurance—

Mr. SHERMAN. They have committed to do it, but they might change their mind and decide they don't want to do it. But this binds them to it.

Mr. MCRAITH. No, the agreement provides them latitude to supervise as they have done historically and have planned to do publicly. With respect to reinsurance, there is the potential for preemption, but they have adopted that reform as an accreditation standard, meaning every State, including California and Washington, has to adopt it as a matter of law or regulation within the next 2 or 3 years.

Mr. SHERMAN. And what if they choose not to? What if the legislature of California says, we hate everything you did? What happens?

Mr. MCRAITH. Then that State, California, would lose its accreditation status with the NAIC, which would punish California industry and consumers, but that is an NAIC issue.

Mr. NICKEL. Congressman, may I—I'm sorry.

Mr. SHERMAN. Yes, go ahead.

Mr. NICKEL. May I just jump in a little bit? A couple of things. One, yes, we do have an accreditation process. And we will be finished with that accreditation process, where we do have a reinsurance law on the books. But our reinsurance law does not go to zero, unless there is an extraordinarily well-capitalized company.

We will be preempted and we will be asked to change our law to the law that will already be in effect in most States to recognize the fact that we either need to change it or to be preempted.

Mr. SHERMAN. And as Mr. McRaith pointed out, if you choose not to do that, you and your consumers and your companies will be punished through an act of the U.S. Federal Government? Do I have that right?

Mr. MCRAITH. That would be an act of the States.

Mr. NICKEL. There would be preemption, yes.

Mr. SHERMAN. Excuse me. Go ahead.

Mr. NICKEL. That would be the preemption piece, that—if a State decides not to comply.

Mr. SHERMAN. If a State chooses not to comply, what—Mr. McRaith was saying that results in the consumers and/or companies in that State suffering. How would they suffer?

Mr. NICKEL. In my opinion, we all suffer by having the—if we focus on the reinsurance collateral piece a bit, for just one more second, that we lose the reinsurance collateral provisions of our model. There are 216 reinsurers in the European Union. Only six of them have gone through our process to reach financial security review, financial stability review. The other ones haven't. They are at 100 percent collateral.

When this goes into effect, the other two hundred and whatever go—216 go from 100 to zero. But right now, they are operating fully comfortable at 100 percent collateral. So just so we are clear, this isn't just a couple of companies wanting to do business in the United States. We will have a large number of European reinsurers now operating in the U.S. that didn't either want to follow or chose not to follow our financial review.

Mr. SHERMAN. Ms. Pusey, do you regard this as a threat to our State-based system of regulation? I know that you have generally taken the view that this is a win-win. So why is it a win for the concept of State regulation?

Ms. PUSEY. Because it really enshrines it. It preserves it. So we took a contrary view, because we actually see that this does not threaten the State-based system. It actually preserves it. I don't know whether we wore the Europeans out over time or what has happened. They certainly have had an interest in exporting Solvency II to other jurisdictions. That is very true. And it is also very true that the U.S., from industry perspective and regulator perspective and Federal Government perspective, has said no to that and have resisted it.

So for whatever combination of reasons, late this fall, there was a wearing down, if you will, in the deal—from a product—if you look at the results, our view is that this is respecting the U.S. system. It is going to let us regulate ourselves under our group supervisory rules and our group capital rules.

Mr. SHERMAN. I yield back.

Chairman DUFFY. The gentleman yields back. The Chair now recognizes the gentleman from California, Mr. Royce, for 5 minutes.

Mr. ROYCE. Thank you, Mr. Chairman. I know in my committees, there is a practical limitation. I usually only have three or four witnesses. But in this particular case, if we are going to have a full conversation about this agreement, we do need to think about all the negotiating parties and all the parties affected that are not at the table, the USTR here, the life insurers, the reinsurers, the major brokers.

And the practical limitations don't allow us really to make the hearing that broad. But I would make that point. And if I could summarize where I think we are today, in terms of these tracks, on the one hand, the States are going down a path where reinsurance collateral requirements are already being lowered, albeit at a snail's pace, and in return the E.U. has not agreed to any relief for U.S. insurers or reinsurers. It is possible we get nothing then for something. So that is one path.

And meanwhile, Congress gives Treasury and the USTR the power to negotiate a covered agreement, a power, by the way, which was debated in this very committee and unanimously supported by both sides of the aisle on a bipartisan basis. Treasury and the USTR then negotiated an agreement that effectively agrees to what the States have already agreed to do and lower the reinsurance collateral.

In return, we open up the entire E.U. reinsurance market to U.S. reinsurers without discrimination and we save direct writers billions of dollars in European compliance costs, which as we have heard today can be passed along to consumers.

So I would just ask Ms. Pusey, am I missing something here in the way this appears to me?

Ms. PUSEY. No, sir, that is our read, as well.

Mr. ROYCE. And I would ask Mr. McRaith, without this agreement in place, we have seen regulators in the U.K. and in the Netherlands, Austria, Germany, and Poland place U.S. companies at a severe disadvantage. If we scrap this agreement, as some are suggesting today, where does that leave us? And what are State regulators authorized to do to adequately address these issues? Is the E.U. looking to sign MOUs with 50 States?

Mr. MCRAITH. U.S. reinsurers were being denied opportunities 9, 10 months ago in the E.U. We resolved that issue through the agreement and opened the entire European market to U.S. reinsurers. U.S. primary companies were being asked to comply with extraordinary regulatory requirements in the E.U. that could be increasingly burdensome, but for this agreement.

I can't speak to what the Europeans would do in the event this agreement were to fail in the United States. But I know that our industry and American insurance jobs have a lot—our industry has a lot to lose and American insurance jobs are at stake.

Mr. ROYCE. Well, that was my read of the situation, as well, Mr. McRaith. And I will yield back, Mr. Chairman. Thank you very much.

Chairman DUFFY. Thank you. The gentleman yields back. The Chair now recognizes the gentleman from Washington, whom I would just note has a strong interest in protecting our State-based model and has introduced legislation on a similar issue. The gentleman from Washington, Mr. Heck, is recognized for 5 minutes.

Mr. HECK. Thank you, Mr. Chairman. Thanks very much for the opportunity even to participate today.

Mr. McRaith, you and I kind of went back and forth on this quite a bit last year. And I took the position of a protector of State-based regulation. You assured me as a former State regulator that that would be the case verbally, and then you wrote—or your office wrote me a letter that said the law did not require that Treasury and the USTR include State insurance regulators in the negotiations.

Nevertheless, in recognition of the role of States in U.S. insurance oversight, Treasury and the USTR are including and engaging with State regulators in a direct and meaningful manner throughout the ongoing negotiations.

And I take it from your earlier somewhat impassioned remarks that you believe that you complied with both the letter and the spirit of that assurance to me. Yes or no?

Mr. MCRAITH. The agreement is a better agreement because State regulators were at the table—

Mr. HECK. Did you comply with the spirit—

Mr. MCRAITH. —in the room. They absolutely contributed.

Mr. HECK. Did you comply with the letter and spirit of what you wrote?

Mr. MCRAITH. Absolutely.

Mr. HECK. Thank you, sir. Mr. Nickel, you said in your opening statement that State regulators were assured that we would have direct and meaningful participation, but the small group of us included were merely observers: only one allowed in the room subject to strict confidentiality with no ability to consult our staff and fellow regulators. Is it fair to characterize your view that the spirit and letter of what was assured to me and which I just quoted was not adhered to?

Mr. NICKEL. I think that is a fair characterization, Congressman.

Mr. HECK. And, Mr. Nickel, is it accurate that you are the elected or chosen voice on behalf of the State regulators throughout our country, and you are speaking on their behalf?

Mr. NICKEL. I am speaking on their behalf today.

Mr. HECK. So in addition to that irreconcilable points of view, I would like to quite literally, Mr. Chairman, seek permission to enter into the record the voice of yet another entity, that of the Intergovernmental Policy Advisory Committee on Trade (IGPAC), a letter from the Chair of IGPAC. May I, sir?

Chairman DUFFY. Without objection, it is so ordered.

Mr. HECK. So IGPAC, as you may all know, is the trade advisory committee appointed by the USTR, and it provides trade policy advice on matters that have a significant relationship to the affairs of State and local governments. I think this is significant, because it is a voice actually beyond insurance regulators, per se, but on behalf, as it were, the corporate interest of State Government.

And I want to, if I may, quote briefly from the letter that I am in receipt of from the Chair, Mr. Robert Hamilton, "After it was reported that the U.S. and the E.U. were negotiating a covered agreement, on multiple occasions, the IGPAC requested that the USTR and the Treasury Department closely consult with the relevant stakeholders and provide regular briefings to the IGPAC throughout the covered agreement negotiations in light of the potential for this agreement to impact State sovereignty, discriminatory actions by E.U. member countries, and potential national treatment violations by the E.U. Unfortunately, the Treasury Department and the USTR failed to honor this promise and provided only one superficial briefing in December 2015 before the first round of negotiations and failed to provide any briefings during the ongoing negotiations."

Mr. Chairman, I would submit not just this letter, but fact that the preponderance of evidence is, in fact, on the side of those who believe that the process did not meaningfully involve the State regulators and those who had that interest at stake. But look, I don't seek to protect State-based regulation for its own sake in and of itself. Good process, bad process, evidence suggests bad process. Good product, bad product, arguable. I do so because, in fact, what we have observed is an undercutting of the State-based regulation.

And that to me is harmful in two ways. Number one, it is violative in spirit, if not technically, of the underlying policy framework of insurance regulation in this country, namely the McCarran-Ferguson Act. And let me remind everybody that the basic covenant of McCarran-Ferguson is that if you will to submit to State-based regulation, you are exempt from antitrust.

I strongly suspect—I am not even going to ask, Ms. Pusey—that you do not want to have our antitrust exemption pulled from you. But if McCarran-Ferguson is no longer the law of this land, directly or indirectly, that is exactly the debate we ought to have.

And secondly, I protect State-based regulation because it works. Because we provide good safety and soundness regulation, prudential regulation, and consumer regulation. And if you are asking who is better to do this, the Feds or the States, I just want to remind you that AIG was regulated by the Feds. How did that work out for us?

State-based regulation works. And we should not go down the path of that which undercuts it. With that, I yield back the balance of my time, and I thank you, Mr. Chairman.

Chairman DUFFY. The gentleman yields back. The Chair now recognizes the gentleman from New Jersey, Mr. MacArthur, for 5 minutes.

Mr. MACARTHUR. Thank you. Before I get to my questions, I would actually like to ask Ms. Pusey if you would answer that question. Would you like to see your members be subject to antitrust regulation and see McCarran-Ferguson overturned?

Ms. PUSEY. Thank you for that opportunity. We are very strong supporters of the State-based regulatory system. We have no interest in supporting and have arduously opposed any efforts to undermine State-based regulation. And it is in that spirit that we can support this agreement, because we think it actually recognizes it and props it up and gives it global recognition.

Mr. MACARTHUR. But you would not want to see your position relative to antitrust changed?

Ms. PUSEY. No, sir.

Mr. MACARTHUR. Your members wouldn't want that?

Ms. PUSEY. Congress delegated that authority to the States from McCarran. Yes, sir, we appreciate that recognition on the antitrust.

Mr. MACARTHUR. Mr. Nickel, could you—and you could go on for a while, but I need you to be brief—

Mr. NICKEL. I will try.

Mr. MACARTHUR. —because I don't want to have to cut you off, and I have a few other questions. Could you very briefly remind us of the benefits of State-based regulation to consumers?

Mr. NICKEL. Sure. We are the boots on the ground representing consumers in front of insurance companies. When there are issues, we work in their States. We know them by name. They call us. We take care of consumers. And then we ultimately take care of and monitor the financial solvency of the companies domiciled in our State.

Mr. MACARTHUR. When an insurer fails, is it fair to say that the home State is generally the one that is impacted the most?

Mr. NICKEL. Generally speaking, yes. But sometimes companies have a broad footprint throughout many States.

Mr. MACARTHUR. I understand. But generally, it is local people, another reason I think for State-based regulation. I want to explore this idea of preemption. Mr. McRaith, I thought your answer before was really very interesting. And I am paraphrasing, so correct me if I didn't get this right, but you said that this doesn't regulate industry participants; it controls how the regulators oversee those participants or impacts. Is that basically what you said?

Mr. MCRAITH. It is an agreement of mutual respect, where the E.U. says, "U.S., you do it how you want to do it." And we say to the E.U., "You can do it how you want to do it."

Mr. MACARTHUR. But what happens if an insurer, an individual, not a group, but an individual writer of insurance in a State has a different opinion of what it needs to hold in capital and the regulator in that State agrees with the capital requirement? What happens if that is different from what the FIO believes should be held or what the E.U. regulators believe should be held? Whose opinion carries the day on how much capital needs to be held?

Mr. MCRAITH. The only party authority relative—that can determine whether a U.S. insurance company has sufficient capital is a State regulator. And this agreement endorses exactly that.

Mr. MACARTHUR. Is there any circumstance where the covered agreement could preempt a State's determination of capital requirements?

Mr. MCRAITH. No. The group supervision practices, including the—

Mr. MACARTHUR. So what is the 5 years that a State regulator has to comply—what does that apply to?

Mr. MCRAITH. So for over 2 years, the States have been developing a group capital calculation. The agreement gives them an additional 5 years to do that for the insurers that are operating—only the insurers operating both in the U.S. and the E.U. So not every company, not every State, not every company in any State.

Mr. MACARTHUR. But those are the very ones I am asking you about. So if there is a difference of opinion with one of those groups, whose determination prevails?

Mr. MCRAITH. It is the State regulator who will decide how companies are regulated. If hypothetically, to the Chair's question earlier, if the E.U. has a different view of that, and the adequacy of that, that is discussed. Supervisors, by the way—as you well know—deal with these issues every day. These are nuts and bolts regulatory questions dealt with—

Mr. MACARTHUR. I have to cut you off, because I have only 30 seconds. And I just want to make a point. Where you stand on this issue I suspect depends on what your business interests are. It is sort of, "whose ox is being gored."

So I understand why the insurance commissioners see it as an erosion of their control. I understand why the mutual companies—and I was once a member of NAMIC and was once a member of AIA—so I understand both—and AIA's members, unless it is changed, are companies like Munich Re, Swiss Re, Allianz. These are global insurers. And so it is no surprise to me that your members welcomed this sort of a change in the oversight, because your members are very different than NAMIC's members. Is that not true?

Ms. PUSEY. Hartford, Travelers.

Mr. MACARTHUR. I know that there are those. But two-thirds of your board members are global insurers.

Ms. PUSEY. No, with all due respect—

Mr. MACARTHUR. I know, because I checked. I checked this morning. So it is not meant to be a criticism. It is just the reality that your perspective is very open to this shifting to a globalization of insurance control. And I don't think that comports at all well with McCarran-Ferguson and the State-based system that has served us so well.

My time has expired. I yield back.

Chairman DUFFY. The gentleman yields back. The Chair now recognizes the gentleman from Illinois, the vice chairman of the Capital Markets Subcommittee, Mr. Hultgren, for 5 minutes.

Mr. HULTGREN. Thank you, Mr. Chairman. And thank you all so much for being here today. I appreciate your work.

Director McRaith, it's good to see you. We worked together in Illinois and also out here, as well. And I appreciate all of you being here today.

I am new to the Housing and Insurance Subcommittee. I am grateful to be working with Chairman Duffy and everybody else. I think this is so important. And especially for Illinois. We have a lot of challenges in Illinois. One of the things we actually do well is insurance. And I have some wonderful entities there and I am grateful for them, but I am also grateful for the work that they provide to my constituents. So these are important issues that we are discussing.

Illinois, as I said, has a number of insurance companies that are vital to ensuring customers. Consumers and businesses are able to manage their risk in all of their endeavors. Today's topic regarding the recently negotiated covered agreement between the U.S. and the E.U. is an important one, and I am glad Chairman Duffy worked expeditiously to convene this hearing in the 90-day review period provided to Congress.

Mr. McRaith, I wonder if I could address my first question to you: Does the covered agreement require States to change collateral rules? And if so, this is only perspective, correct? Is that true? And would existing reinsurance contracts be affected?

Mr. MCRAITH. The agreement would potentially require States to do what they have already committed to doing with respect to reinsurance collateral reform. Period. And I'm sorry. Your second question?

Mr. HULTGREN. Would existing reinsurance contracts be affected?

Mr. MCRAITH. Oh, I'm sorry, yes.

Mr. HULTGREN. But let me finish. The text of the covered agreement says amended reinsurance contracts could be impacted by the agreement. Can you clarify this definition and explain what effect an amendment to a reinsurance contract would have on reinsurers' obligation to post collateral?

Mr. MCRAITH. Yes, exactly. The agreement is clear that it only applies prospectively. Questions come up about what does the word "amendment" mean? First of all, an amendment to a contract requires two parties to agree, so if the ceding insurer doesn't agree, there is not an amendment to the contract.

However, if there were an amendment, in this context, that would have to be a material change to the underlying reinsurance contract. It could not be just some clerical or administrative change. It would have to be a meaningful material change to the underlying contract.

Mr. HULTGREN. Okay. Staying with you, Mr. McRaith, I wonder if you could walk me through the process of how this covered agreement was negotiated. As someone who served as a former insurance commissioner of Illinois, your perspective certainly is important to me and valuable to me. What role did the State of Illinois have in negotiating the covered agreement? And if they did not have a seat at the table, who was speaking on their behalf, and what mechanism for input did they have?

Mr. MCRAITH. We began the negotiations actually in early 2016 after announcing the start in late 2015. We asked the States to identify the membership of a small task force that would participate directly in the negotiation. As a former State regulator, and as the Director of the Federal Insurance Office, I have said repeatedly, written repeatedly, and strongly believe that McCarran-Ferguson serves our consumers and our industry, our country very well. This agreement is intended to further support that.

So we did get the perspective of Illinois, but the States opted—they chose who the membership of their task force would be. Illinois was then represented by Commissioner Ted Nickel and his colleagues in the effort.

Mr. HULTGREN. Commissioner Nickel, going to you, what role do you feel like you and other State insurance regulators had in the covered agreement process? Since the covered agreement process is new, can you tell us how it compared with other international discussions where State insurance regulators are involved?

Mr. NICKEL. Sure. I will try to be brief. Thank you for the question. I have just met your new Director, Director Hammer. She is great. I think you will be well-served. The statement was made that we selected a group to represent the NAIC. We negotiated a group to be—that not everybody that we wanted to have at the table with us was allowed. We did negotiate a group. It was a small group.

There were seven of us at the table. We would have loved to share updates with interested parties and—there were seven of us. There are 13,000 insurance regulators working every day in the United States that we represent. There were seven of us allowed at the table. Actually, there were seven of us allowed, normally just one at the table.

The process itself was difficult. And it would have been better served if we would have been able to have more ability to share opinions with our members and bring back more thought to the process.

Mr. HULTGREN. I wish that could have happened, as well. My time has expired. We do have a few more questions, so we may follow up with you in writing to see if we could get answers to them. With that, I yield back, Mr. Chairman. Thank you.

Chairman DUFFY. The gentleman yields back. I want to thank our panel for their testimony today. And maybe just to note, it is pretty clear we have a wide array of views on this covered agreement. And it is good for us to hear everyone's different positions. And I think it was Mr. MacArthur who mentioned your business model might dictate your support or lack thereof. And it is good for us to hear from you all.

I also think it is important to note that there may be a need for us as we move forward to look at clarification. I know Mr. McRaith might disagree with that, but I know others have agreed with the clarification point. There has been concern about the process that was used. And there is concern about preemption. And I think you heard unanimous concern for the congressional involvement, should there be any future deals that are put together. Just a couple of my takeaways.

But I think all of us are engaged in this issue, and I look forward to working with not just the panel, but also those who participated, who have shown up to this hearing. So again, thank you all.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And without objection, this hearing is now adjourned.

[Whereupon, at 12:04 p.m., the hearing was adjourned.]

A P P E N D I X

February 16, 2017

NAMIC®
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Statement

of the

National Association of Mutual Insurance Companies

to the

United States

House Financial Services Subcommittee

On Housing and Insurance

Hearing on

Assessing the U.S.-EU Covered Agreement

February 16, 2017

The National Association of Mutual Insurance Companies (NAMIC) is pleased to provide comments to the House Financial Services Subcommittee on Housing and Insurance on the recently completed U.S.- European Union (EU) covered agreement dealing with insurance regulation. We appreciate the subcommittee's focus on an important matter that has the potential to greatly impact the domestic U.S. property/casualty insurance industry.

NAMIC is the largest property/casualty insurance trade association in the country, with more than 1,400 member companies representing 39 percent of the total market. NAMIC supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers. NAMIC member companies serve more than 170 million policyholders and write more than $230 billion in annual premiums. Our members account for 54 percent of homeowners, 43 percent of automobile, and 32 percent of the business insurance markets.

Introduction

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) created a new office in the Department of Treasury called the Federal Insurance Office (FIO). Although given no explicit regulatory authority, the new office was empowered, in conjunction with the United States Trade Representative (USTR), to negotiate and enter into international "covered agreements" on insurance regarding prudential measures. These agreements are between the U.S. and one or more foreign governments or regulatory entities and must "achieve a level of protection for insurance or reinsurance consumers that is substantially equivalent to the level of protection achieved under State insurance or reinsurance regulation."

The "covered agreement" concept was wholly created by and defined in the Dodd-Frank Act. It is an invented term for insurance and not a standard type of contract, covenant, understanding or rule, subject to existing and recognized practices and requirements. The scope of a covered agreement is not well-defined in statute, but the Dodd-Frank Act provided the power to preempt state insurance laws that are inconsistent with the agreement and result in less favorable treatment of a non-U.S. insurer domiciled in a foreign jurisdiction that is subject to a covered agreement. Exactly how these agreements are to be negotiated, entered into, and applied are subject to interpretation of the high-level guidelines in Dodd-Frank. Many questions remain concerning these agreements, the policy decisions at the outset and throughout negotiations, as well as the application of these agreements, and the rights of parties to participate in and/or challenge them.

NAMIC has long had serious concerns about the use of an international trade negotiation process to alter or preempt the state-based system of insurance regulation. We have argued that the USTR and the FIO should exercise such authority only if they determine that extreme circumstances demand it, and then only after full and transparent due process, including consultation with state legislative and regulatory authorities and public exposure of the policy objectives of the negotiations.

Our analysis of the recently finalized draft agreement validates our long-held concerns. Despite claims otherwise, we believe that the covered agreement does not address the problems the FIO and USTR committed to resolve when the negotiations were started. To be clear, those companies that are being threatened by increased regulatory burdens by EU regulators need relief and we are in favor of providing them with that relief. However, the agreement is ambiguous and unclear and does not provide sufficient protections and benefits for the U.S. insurance market and consumers. As drafted the agreement represents a bad deal for the U.S. domestic property/casualty insurance industry. The U.S. can – and must – do better.

Currently, the agreement sits in Congress for a 90-day layover period, which is intended to provide lawmakers the opportunity to review and provide comment on the agreement. However, the agreement does not require congressional approval. At the end of the 90 days, Treasury and USTR may bring it into effect. This 90-day period began to run seven days before the new President was inaugurated, before the new Treasury Secretary or U.S. Trade Representative was confirmed, and after the key U.S. negotiators had resigned their positions. That said, Congress should urge the Trump Administration to go back to the drawing board and secure a better deal.

Covered Agreement Negotiations

On November 20, 2015, the FIO and USTR officially sent a letter to Congress announcing the initiation of negotiations for a covered agreement between the U.S. and the EU, notification required by Dodd-Frank. Over the course of a year, representatives from the U.S. and the EU met five times in person for negotiations. These meetings were followed by a series of telephone negotiations at the end of President Obama's second term. Finally, in the last week of the Administration, on Friday, January 13, 2017, USTR and the FIO released the final negotiated covered agreement language.

The impetus for the initiation of negotiations was the pending 2016 implementation of the EU's insurance regulatory reform known as Solvency II. Under the new regime, an insurer doing business in the EU is subjected to heightened regulatory and capital requirements in the event that the insurer's country of domicile is not deemed "equivalent" for purposes of insurance regulation. U.S.-based insurers had begun receiving threatening letters from EU regulators suggesting that because the U.S. had not been deemed equivalent, they stood to be penalized which would make them less competitive. While this created a real and present difficulty for the small number of insurers doing business overseas, the need for "equivalency" was completely manufactured by the EU in their enactment of Solvency II.

It is likely that the EU leveraged its Solvency II equivalency determination to pressure the U.S. to negotiate more favorable treatment for its reinsurers. Foreign-based reinsurers have long chafed at the requirement in the states that they must post collateral in the U.S. for ceding insurers to get credit for purchasing their reinsurance. This problem was addressed by the NAIC in their 2011 revised model Credit for

Reinsurance Act. In that model act they provided for a staggered collateral system based on the credit rating of foreign reinsurers from qualified jurisdictions. Despite the passage of that model in more than 35 states, the goal of the EU has always been to quickly and uniformly eliminate the requirements for reinsurance collateral in the U.S. for the benefit of EU reinsurers.

Whatever the case, many of the U.S. companies that do business internationally urged the FIO and USTR to move quickly to negotiate a covered agreement with the primary goal to settle – promptly and finally – the question of U.S. insurance regulatory equivalence with the EU under Solvency II. With the two sides' goals in mind, the 2015 letter announcing the initiation of negotiations laid out the prudential measures the covered agreement would seek to address:

1. Obtain treatment of the U.S. insurance regulatory system by the EU as "equivalent" to allow for a level playing field for U.S. insurers and reinsurers operating in the EU;
2. Obtain recognition by the EU of the integrated state and federal insurance regulatory and oversight system in the United States, including with respect to group supervision;
3. Facilitate the exchange of confidential regulatory information between lead supervisors across national borders;
4. Afford nationally uniform treatment of EU-based reinsurers operating in the United States, including with respect to collateral requirements;
5. Obtain permanent equivalent treatment for the solvency regime in the U.S. and applicable to insurance and reinsurance undertakings.[1]

As we will discuss in more detail below, even by the standards laid out by USTR and the FIO the negotiated covered agreement is a failure for the United States. There is no finding that U.S. group supervision is permanently adequate, mutual, or equivalent. The EU has only agreed to return to pre-Solvency II status quo when they were not unfairly punishing U.S.-based insurers for the U.S. state laws.

The Covered Agreement

The covered agreement allows for a period of five years to phase-in provisions which address three prudential areas – Reinsurance Collateral, Group Supervision, and Confidential Exchange of Information. The agreement also sets up a permanent "joint committee" to oversee implementation and to consider amendments in the future. NAMIC believes that on the whole there are more negative provisions than added value especially for those insurance companies that only write in the U.S. For companies writing internationally who need to rely on this agreement the most, its ambiguity raises significant questions about what they can count on from the EU insurance supervisors, if U.S. regulators will meet the obligations they were not involved in negotiating, and whether they will be disadvantaged by one of the many exceptions to the agreement.

[1] November 20, 2015 letter from the U.S. Treasury Department and the Office of the United States Trade Representative to Congressional Committee leadership announcing initiation of covered agreement negotiations with the European Union.

These companies and those who represent them are "hopeful" things will work out and they want to believe that everyone will abide by the intent of the agreement. NAMIC is not so optimistic. We believe we can only rely on the language in the four corners of the document, and that language is not encouraging.

Reinsurance Collateral

The section of the covered agreement dealing with reinsurance collateral states that no EU reinsurer, meeting all other requirements to do business in the U.S., can be required to post collateral in the U.S. If the states do not adopt laws reflecting this zero-collateral requirement within five years, the covered agreement allows the federal government to pre-empt those state laws which remain in conflict.

Of course, this change will negatively impact insurers, both small and large in the U.S. as these companies are no longer guaranteed the collateral that EU reinsurers must hold in the U.S. to assure prompt payment of reinsurance claims. This collateral is critical to assure the collectability of U.S. judgments. Reinsurance payments help insurers timely pay the money owed to policyholders in the event of natural catastrophes or other large loss events. The elimination of required collateral particularly disadvantages smaller insurers which are more reliant on reinsurance. And though the agreement provides no prohibition on negotiating for collateral in reinsurance contracts, the small insurance companies will not have the same negotiating power as larger companies.

With the elimination of reinsurance collateral, state regulators have already proposed to eliminate credit to the companies for the purchase of reinsurance. Instead they would replace the lost reinsurance collateral by creating new obligations for the ceding companies in an enhanced capital requirement. This would fundamentally alter the way all U.S. insurance companies deal with capital requirements.

We do not dispute some potential benefit from the resolution of the reinsurance issues between the U.S. and the EU. However even those benefits are exaggerated and in many cases impacted by exceptions and ambiguous language.

First, there is a claim that the elimination of collateral requirements could result in lower reinsurance premiums. Premiums are affected by market cycles and currently the soft market driven by a flood of new capital is causing prices to go down particularly in the property catastrophe reinsurance market. In addition, the enactment of the NAIC's model law in many states and the collateral reduction that resulted may have already contributed to lower prices. Second, there are provisions which increase the requirements applicable to the EU reinsurers for ensuring payment of claims owed and enforcing judgments in the U.S. These are positive provisions, but would be unnecessary if not for the covered agreement removing the collateral requirement. Finally, the EU supervisors can no longer require U.S. groups doing business in EU member states to have a "local presence" in the country unless they have a similar requirement for their domestic (re)insurers. While U.S. (re)insurers are considering this an important concession, this is only an advantage for U.S. groups doing business in the EU if the EU supervisor does not currently have, nor decides to add, a similar requirement for the domestic EU companies. In addition, it is important to note that if the agreement fails or terminates, it would be much easier to undo forbearance of these local presence demands of of EU supervisors than to repeal new state laws/regulations eliminating reinsurance collateral. **This is not an equal trade for U.S. insurers**.

The EU is unlikely to be the last jurisdiction to push for zero-collateral requirements as Bermuda has already asked whether the U.S. will give them the benefit of the same deal. This could be the beginning of zero collateral for all non-U.S. reinsurers. This would ignore the work state regulators/legislatures have done in the last several years in adopting changes to the NAIC's Credit for Reinsurance Model Act and Regulation. The state policymakers enacting these laws have considered the issues, listened to interested parties, and developed solutions that balance the interests of foreign reinsurers, the U.S. primary insurers that are their customers, and the policyholders of U.S. companies who expect their claims to be paid. The process has been methodical and transparent and the issues fairly and openly debated, unlike anything about the covered agreement. Thirty-five states have already acted to enact this new NAIC model and those remaining states need to enact the revised model before 2019 to retain their NAIC accreditation.

Group Supervision

The covered agreement also addresses group supervision and group capital requirements. This issue was added to the covered agreement by U.S. Treasury with the idea that the U.S. would gain acceptance of the U.S. existing system of group supervision in exchange for giving up reinsurance collateral. Observers and interested parties were expecting simple recognition of the supervision provided in the model holding company act adopted and enforced in all states.

Instead, the agreement provides that the EU will allow U.S. insurance regulators to provide group supervision for their own domestic insurance groups that do business internationally. But, the EU doesn't recognize this right for parts of U.S. holding companies based in the EU or any of the affiliates of that EU-based group anywhere in the world. The EU also does not recognize this right for any U.S. holding company with a depository institution or that has been designated a Systemically Important Financial Institution (SIFI) or Global Systemically Important Insurer (G-SII). Nor does the agreement recognize this right if at any time they feel the insolvency of one of these U.S. companies could harm EU policyholders or threaten the EU economy. Finally, even if the U.S. provides supervision the EU maintains the right to ask for "information" for purposes of prudential group supervision that is "deemed necessary" by the EU supervisor to protect against serious harm to policyholders or financial stability. This sounds as though EU regulators can apply Solvency II reporting requirements at their discretion.

In concept, this group supervision provision is what U.S.-based insurers doing business in the EU need to avoid punitive regulatory requirements from EU supervisors. However, once the U.S. meets all its obligations under the agreement, and all the exceptions to the "recognition" of group supervision are considered, there is no language requiring that the EU will treat the U.S. as a "mutually recognized" or "equivalent" jurisdiction under Solvency II. Under this agreement, the U.S. will be taking actions at the state level that will be very difficult to reverse, without any guarantee that at the end of five years the EU would continue to recognize the U.S. insurance regulatory structure as permanently mutual or equivalent. Allowing U.S.-based insurers to continue operating in the EU without regulatory penalty is nothing more than a return to the pre-Solvency II status quo. Even by the standards laid out by USTR and the FIO, this provision is a failure.

Of perhaps the greatest concern for all U.S.-based insurance groups (internationally active or not) is that the covered agreement seems to require U.S. states to enact provisions that are at odds with the U.S. legal entity system of regulation, specifically a group capital requirement. If these group capital standards are not adopted, the EU will not live up to its side of the agreement, but if they are adopted, it will impact even those companies not doing business in the EU.

Article 4(h) requires the U.S. to impose a group capital assessment that sounds similar to an NAIC project underway to develop a group capital calculation that has specifically been designed as a tool for supervision, not a capital requirement. However, the covered agreement anticipates a calculation that is more than an assessment tool. It must apply to the complete "worldwide parent undertaking" and ***must include corrective/preventive measures, up to and including capital measures***. It appears that the intention is to include the power to require increases in capital, capital movement between affiliates, or other fungibility mandates. Implementation of this kind of group capital standard will shift the U.S. away from a legal entity regulatory system and toward an EU-style group supervision system. ***Capital additions and new requirements will affect the affordability and availability of new insurance products and are not in the best interests of consumers.***

As noted these capital requirements would apply to the "world-wide undertaking parent" or the entire conglomerate that holds an insurance company – even entities completely removed from the insurance and financial sectors. This scope of capital is not even required under Solvency II, is broader than the scope of the current IAIS group capital standard, and conflicts with common sense. Insurance regulators should not be assessing the risk of manufacturing affiliates, telecommunication companies, and hotels held by a conglomerate just because they also hold an insurance company. This is, rightfully, outside their authority.

It is not clear that it was the intention of the parties to apply the covered agreement preemption authority to the group supervision provisions. However, the plain language of the agreement (Article 9) suggests it is not limited to the reinsurance article of the agreement. The Dodd-Frank Act states that the Director may only apply preemption to a state law that:

> "(A) results in less favorable treatment of a non-United States insurer domiciled in a foreign jurisdiction that is subject to a covered agreement than a United States insurer domiciled, licensed, or otherwise admitted in that State; and (B) is inconsistent with a covered agreement." (31 USCS §313(f)(1)(A) and (B))

Some interpretations provide that this language limits application only to the reinsurance requirements. But there is concern that the EU may expect the groupwide supervision language in the 2014 NAIC Holding Company Model Act to be adopted in every state. If that is the expectation, it could lead to a nullification of this agreement down the road – after the U.S. has already enacted difficult to reverse changes to state insurance law and regulation.

Process Concerns

NAMIC has serious concerns both about how the current covered agreement was negotiated, and how the process will work going forward. Negotiations with the EU were conducted in closed, confidential meetings, between the EU Commission, USTR, and the FIO. State insurance regulators were relegated to a minimal role, though these negotiations directly and significantly impact state laws and regulations. In the letter announcing negotiations both USTR and the FIO stated that "State insurance regulators will have a meaningful role during the covered agreement negotiating process."[2] Both offices clearly failed in this commitment – only a small group of state regulators were included in the process as mere observers and were subject to strict confidentiality with no ability to consult fellow regulators or the broader community of stakeholders.

Going forward, we are concerned about the creation of a standing "joint committee" composed of unnamed EU and U.S. representatives to oversee both implementation and the amendment of the current agreement. There may be some benefit from having a formal committee to help address disputes among the parties regarding the agreement. However, the joint committee creation and required meetings once or twice a year add to the perception that this is intended to be an on-going evaluative process with the EU and U.S. federal authorities telling state regulators whether they are doing their jobs well enough to meet federal and EU standards. The amendment process built into the agreement also conceivably allows federal and EU authorities to alter the terms in such a way that could also lead to further preemption of state law. And these amendments could be made without entering into a "new" covered agreement, bypassing the transparency provisions like the 90-day lay-over period put in place in Dodd-Frank. The prospect of endless renegotiation with the EU with little in the way of transparency should be worrisome to all.

Conclusion

The letter announcing the commencement of negotiations with the EU, clearly stated that "Treasury and USTR will not enter into a covered agreement with the EU unless the terms of that agreement are beneficial to the United States."[3] NAMIC does not believe that the offices met this criterion. Overall, the deal is a bad one for the vast majority of U.S. insurers which do not have operations in Europe and which get nothing from the agreement other than increased costs and new regulatory uncertainty. It is also a bad deal for consumers in America who ultimately pay for all of the additional costs associated with EU-style regulation being imported to the United States.

The covered agreement is an invented solution to an invented problem – the question of European regulators deeming our regulatory system equivalent. Again, to be clear,

[2] Ibid.
[3] Ibid.

those companies that are being threatened by increase regulatory burdens by EU regulators need relief and the U.S. should find a way to provide them with that relief. However, it is our view that the U.S. can and should explore other ways to address the unjustifiable trade barriers which the EU seems intent on throwing in the way of our domestic insurers attempting to do business overseas. That might include recourse through existing enforcement tools available in trade agreements, or it might involve negotiating a mutual recognition provision in a future trade agreement. NAMIC believes that the U.S. ought to be able to move the EU to take non-equivalent determinations off the table so that our insurance and reinsurance markets can continue to function without unfair barriers to trade.

In the end, Congress should urge the Trump Administration to go back to the drawing board and secure a better deal. A new solution is needed that meets the needs of the insurance-buying public, the insurance industry, and state regulators. NAMIC appreciates the opportunity to testify and looks forward to working with the committee going forward.

EMBARGOED FOR DELIVERY

Written Testimony of Michael T. McRaith
House Committee on Financial Services
Subcommittee on Housing and Insurance
"Assessing the U.S. - EU Covered Agreement"
February 16, 2017

Chairman Duffy, Ranking Member Cleaver, members of the Committee, thank you for inviting me to testify about "Assessing the U.S. - EU Covered Agreement."

I previously served as the Illinois Director of Insurance from 2005- 2011, and as the Director of the Federal Insurance Office (FIO) at the U.S. Department of the Treasury from 2011 until January 20, 2017. While serving as the FIO Director, among other things, I coordinated and developed Federal policy on prudential aspects of international insurance matters and served as Treasury's lead negotiator for the "Bilateral Agreement Between the European Union and the United States of America on Prudential Measures Regarding Insurance and Reinsurance" (Covered Agreement).

Including today, I have been privileged to testify before Committees of the United States Congress on 20 occasions. I first testified on June 20, 2006, on behalf of the National Association of Insurance Commissioners (NAIC) in the U.S. Senate Committee on the Judiciary, and offered testimony in support of the limited anti-trust exemption in the McCarran-Ferguson Act. As in that first hearing, and in every hearing since, I reiterate today my respect and support for the U.S. integrated system of insurance oversight wherein the states remain the primary regulators of the business of insurance.

Most states have diverse insurance markets in which multi-national insurers of great size, scale and complexity compete against insurers that operate only in one state, or in only one region of one state. As the Director of Insurance in Illinois, I witnessed firsthand the importance of these insurers — regardless of size or geographic reach — to consumers, to local and state economies, to employees, and to our national interests. Insurance agents, brokers and companies are an essential feature of every American community.

Competitive insurance markets offer critical benefits to working families and small businesses. Products and services offered by America's insurers allow families to protect and accumulate property, to transfer wealth between generations, and to ensure a financially secure retirement. Insurance is a necessary component of America's promise of economic fairness and opportunity.

Indeed, Treasury and USTR's Covered Agreement negotiating authority recognizes the global interests of the U.S. insurance sector and the implications of those interests for the American insurance industry and consumers. For these reasons, among others, Treasury and the United States Trade Representative (USTR) jointly negotiated and agreed upon the Covered Agreement with the European Union (EU).

Covered Agreement – Background

The prudential insurance matters resolved by the Covered Agreement are neither new nor surprising. Reform of the U.S. state reinsurance laws was first debated by state regulators in 1999, if not earlier, well more than a decade before state regulators unanimously adopted modernized model laws and regulations in November 2011.

However, despite energetic efforts by the state regulators through the NAIC, only 32 states have adopted some version of reinsurance reforms. Both the content and the implementation of that reform varies across those 32 states. For this reason, among others, state regulators, through the NAIC, opted in 2016 to promote consistency in solvency oversight by adopting reinsurance reforms as an NAIC accreditation standard, effective January 1, 2019. By virtue of this NAIC decision, all states will adopt a law or regulation substantially similar to the NAIC model law and regulation by January 1, 2019, or confront the loss of NAIC accredited status.

While the NAIC spent years sorting through alternative approaches to reforms of state-based credit for reinsurance laws, the European Union (EU) spent years developing its Solvency II insurance supervisory regime. Solvency II was first anticipated more than 10 years before its implementation on January 1, 2016. The EU and its member states should be congratulated on the successful technical development and implementation of Solvency II, an EU-wide system of insurance oversight that reflects a high level of professional and political accomplishment.

Almost from the earliest days of the development of Solvency II, U.S. insurance sector participants, including state regulators, were aware that Solvency II could require the EU to evaluate whether non-EU insurers and reinsurers operating in the EU market were domiciled in "equivalent" jurisdictions. An "equivalent" jurisdiction is one, such as Switzerland, which supervises its insurers consistent with Solvency II practices and standards, i.e. global group capital, reporting and governance.

Solvency II and its supervisory approach matter because, in terms of premium volume, the EU's consolidated insurance market is the largest in the world. However, as the world's largest single nation insurance market, U.S. insurance authorities have repeatedly refused to submit to the formal EU Solvency II equivalence process. The United States has long-held that the United States substantively and structurally regulates its insurance sector as the United States determines appropriate, just as the EU determines how to supervise the insurance sector within the EU.

However, the United States has also long known that failure to resolve the Solvency II "equivalence" issue could result in: (1) U.S. reinsurers losing opportunities in the EU reinsurance market, and (2) U.S. primary insurers being forced to satisfy Solvency II global group capital, reporting and governance criteria that are far different, and far more costly, than current regulatory practices in the United States. In the absence of a resolution, U.S. insurers operating in the EU face potentially billions of dollars in Solvency II compliance costs.

As the EU moved to implement Solvency II and U.S. insurance stakeholders learned more about the potential negative impact on U.S. reinsurers and insurers, state regulators continued the massive (albeit piecemeal) effort to reform reinsurance oversight, an initiative that should be applauded for its embrace of a risk-based framework. Nevertheless, in exchange for this reform, state regulators received nothing of benefit for U.S.-based insurers and reinsurers operating in the EU. Nothing.

After difficult and contentious negotiations that began in early 2016, the Covered Agreement will resolve these long-standing issues. The Covered Agreement will remove excessive unnecessary regulation of the global reinsurance industry in both markets, open the EU reinsurance market to U.S. reinsurers, and relieve U.S. primary insurers of potentially billions of dollars in Solvency II compliance costs.

While providing a balanced outcome with an equally meaningful outcome for the EU, the Covered Agreement puts America's interests first. U.S. consumers, industry and the U.S. national economy will benefit because of the Covered Agreement.

Covered Agreement Negotiations — Process and Transparency

U.S. state regulators, most of whom are appointed and serve at the will of a state Governor, have never before been directly included in the negotiating delegation for a U.S. international agreement. In recognition of the unique role of the states in insurance sector oversight, and even though not required by law, the Covered Agreement negotiation process created an unprecedented mechanism for state regulator participation.

Treasury and USTR asked the state regulators to establish a small covered agreement task force of commissioners, and allowed the state regulators to determine the size and membership of the task force.

State regulators were invited to, and did, participate in every Covered Agreement negotiating session.

State regulators were invited to, and did, share perspectives, technical insights, and ask questions during U.S. delegation preparations in advance of any Covered Agreement negotiating session.

State regulators were consulted throughout the Covered Agreement negotiation process, including during any Covered Agreement negotiating session. During the Covered Agreement negotiations, a state regulator sat at the table with the U.S. delegation and frequently provided technical insights.

Through a confidential web portal established for purposes of Covered Agreement negotiations, state regulators received all documents offered by the EU shortly after those documents were received by Treasury and USTR.

Through the same confidential web portal, state regulators received all U.S. Covered Agreement documents before those documents were provided to the EU.

Before any U.S. Covered Agreement document was provided to the EU, state regulators were invited to, and did, participate in a telephone call with Treasury and USTR to provide feedback and insight, and to ask questions. These telephone calls frequently offered important insights and perspectives that were incorporated into, or addressed in, the U.S. Covered Agreement document before that document was provided to the EU.

Prior to my departure from Treasury, both Treasury and USTR expressed appreciation to Wisconsin Commissioner Nickel and his colleagues from California,Texas, Missouri, Florida, Vermont, Tennessee, Kentucky, Maine and Montana for their constructive input and insights provided throughout the Covered Agreement negotiation. These regulators, including Commissioner Nickel, should be commended for contributing substantial time and energy to the Covered Agreement negotiations even while tending to the business of insurance in their home states and to the various NAIC activities in which they are engaged.

In addition, throughout the Covered Agreement negotiations, Treasury and USTR consulted extensively with the four Committees of jurisdiction in Congress. These consultations occurred in person and by telephone, and occurred before negotiations

began, before and after each negotiating session, and before the negotiations and the Covered Agreement were finalized.

Treasury and USTR also extensively consulted with private sector stakeholders, particularly those U.S. insurers and reinsurers with operations in the EU.

Treasury and USTR also worked closely with the entire U.S. Covered Agreement negotiating delegation which, in addition to Treasury and USTR and the state regulators, also included the Departments of Commerce and State, and the Board of Governors of the Federal Reserve System.

This extensive transparency and stakeholder engagement supported and informed the joint Treasury and USTR effort throughout the Covered Agreement negotiations.

Credit for Reinsurance Reform — Removing Excessive Regulation of a Global Industry

The reinsurance industry largely manages risk on a global basis. The reason is obvious: in order to avoid concentration of risk from natural catastrophes, or from a mass epidemic, reinsurers spread capital to different areas and continents. Insurance supervisors support this approach in order to promote affordable and reliable reinsurance markets and, in turn, to promote the affordability and accessibility of insurance products to working families and small businesses throughout the United States.

The Covered Agreement will support the U.S. state-based initiative to reform reinsurance regulation. In fact, the 32 U.S. states that have adopted reinsurance collateral reform already provided collateral relief to 31 non-U.S. reinsurers. Of those 31, 30 now hold 10% or 20% of the collateral required under prior state laws. The state regulators' adoption of the NAIC Model Law and Regulation as an accreditation standard, effective January 1, 2019, means that all states would be expected to adopt a substantially similar reform in the next two years.

If domiciled in a non-equivalent country, a reinsurer operating in the EU could be subject to EU member state laws that require collateral or a local presence. U.S. reinsurers were experiencing this burden in full force: at least two EU member states, with more in process, required that U.S. reinsurers either establish a subsidiary or operate in the EU member state only without the use of brokers. Beginning in mid-2016, U.S. reinsurers were losing existing EU clients and missing new opportunities in the EU.

The Covered Agreement eliminates collateral and local presence requirements for EU reinsurers operating in the United States and U.S. reinsurers operating in the EU, thereby eliminating excessive reinsurance regulation in both markets and establishing a new paradigm for oversight of this essential global industry.

If the Covered Agreement conditions are met, current collateral requirements for EU-based reinsurers will be eliminated within 60 months from the date the Covered Agreement enters into force or, perhaps, as early as mid-2023. U.S states, therefore, have sufficient time within the NAIC's existing plan for accreditation (i.e. January 1, 2019), to conform all state laws to the terms of the Covered Agreement, thereby rendering unlikely the need for FIO preemption of state law.

In addition, if the Covered Agreement conditions are met, current local presence requirements for U.S. reinsurers in the EU (or EU reinsurers in the United States) will be eliminated within two years from the date of signature. Due to the successful conclusion of the Covered Agreement negotiations, EU member states that were imposing local presence requirements on U.S. reinsurers have already agreed to forbear from enforcing compliance.

In addition, by imposing meaningful reporting requirements coupled with the potential for re-imposition of local presence or collateral requirements, the Covered Agreement enhances the protections available to primary insurers and consumers in both the EU and the United States. For example, a reinsurer must confirm in writing that it consents to the jurisdiction of the courts where the primary insurer is domiciled, and must consent in writing to pay all final and enforceable judgments wherever enforcement of that judgment is sought. Also, reinsurers must maintain a practice of prompt payment, and can be required to report to the ceding insurer's supervisor semi-annually with an updated list of all disputed and overdue reinsurance claims outstanding for 90 days or more.

These protections, and the myriad others contained in the Covered Agreement, apply to U.S. reinsurers operating in the EU and to EU reinsurers operating in the United States. In exchange for these enhanced consumer protections, the EU and U.S. reinsurance markets will be open to non-domestic competition in an unprecedented manner, thereby providing free market opportunities that will meaningfully benefit ceding insurers and insurance consumers.

Finally, and importantly, the Covered Agreement provides that U.S. state law and regulation (and EU law and regulation) can revert to its prior form if the Covered Agreement is terminated. Termination of the Covered Agreement will allow for the "snap back" of collateral or local presence requirements, precluding the prospect that the EU or United States could benefit from the Covered Agreement despite failing to comply with its own obligations. *See* Article 3, paragraph 9.

Group Supervision — EU – U.S. Mutual Respect Finalized

The Covered Agreement describes group supervision practices in a manner that accommodates the distinctly different approaches of the United States and the EU. Notably, the group supervision practices of the Covered Agreement apply only to those insurers operating in both the EU and the United States.

Through the Covered Agreement, the EU and the United States acknowledge that supervisors of the jurisdiction in which the insurer or reinsurer is domiciled are the only supervisors with authority to supervise the insurer or reinsurer at the global group level.

The Covered Agreement does not require either the United States or the EU to change group supervision practices. The Covered Agreement does, however, ensure that EU and U.S. regulators can continue with those jurisdiction-specific practices that protect consumers and promote financial stability.

The Covered Agreement group supervision practices memorialize the mutual respect shared by the EU and the United States, and comprise explicit recognition that neither the EU nor the United States will change insurance oversight systems and structures just because of the other. As a factual matter, supervisors in both jurisdictions have adopted, or pursued, practices that originated with the other. For example, U.S. state regulators began development of an Own Risk Solvency Assessment (ORSA) based on the idea as it originated with the EU. Over time, U.S. state regulators adopted the ORSA but in a U.S.-specific way. At the same time, EU supervisors have studied the U.S. state regulators' approach to the collection, compilation and publication of insurance industry data, and are developing a manner and system of insurer reporting that, while different from the U.S. state approach, is premised upon U.S. state-based concepts and practices.

Beginning in 2014, U.S. state insurance regulators, through the NAIC, began development of a group capital calculation for U.S. insurers and reinsurers. This initiative reflects a growing awareness among international insurance supervisors, including at the U.S. state level, that a common group capital standard for multi-national insurers will allow for non-domestic insurance regulators to protect consumers and promote financial stability within their jurisdictions. Although the NAIC group capital initiative has been under development for over two years, it remains in the early phases as state regulators evaluate alternative approaches both to the scope and the technique for the calculation.

It is clear, however, that the NAIC's group capital calculation will not amount to a group capital requirement, and will not require capital to be held by U.S.-based insurers and reinsurers in any place other than the insurance legal entities over which state regulators have authority. The Covered Agreement confirms these two facts, and provides U.S. state regulators with flexibility to build the U.S. group capital calculation on specifications that they determine appropriate. *See* Article 4, paragraph h.

To repeat for clarity, the Covered Agreement only requires that U.S. state regulators proceed with group capital work already underway at the NAIC, and does not specify how that work should conclude. To be abundantly clear, the Covered Agreement would not require that U.S. state regulators develop an approach that requires capital to be held outside of an insurance legal entity, and the reference to "corrective, preventive, or otherwise responsive measures" merely restates existing state-based insurance holding company laws. Indeed, to repeat again for clarity, the Covered Agreement further limits the application of the state regulators' group capital calculation to a much smaller group of U.S. insurers and reinsurers (i.e. only those operating in the EU) than presently contemplated by the state regulators.

Importantly, just as the United States sought respect for the U.S. approach to its group capital calculation, the Covered Agreement is also drafted in a manner that accommodates and expresses respect for the EU approach to a global group capital requirement.

The Covered Agreement limits the application of the EU's Solvency II global group supervision practices to the operations and activities of U.S. insurers that occur in or originate from the EU. While the same limitation of U.S. law also applies to EU insurers operating in the U.S. market, it is the limitation on the application of Solvency II that saves U.S. insurers potentially billions of dollars in additional compliance costs. The savings for U.S. insurers and reinsurers will benefit U.S. insurance consumers through increased affordability, increased insurer investment in the U.S., and more efficient use of the capital that would otherwise be tied to Solvency II compliance.

The Covered Agreement will provide insurers and reinsurers that operate in both the United States and the EU the long-sought clarity and certainty with respect to the relationship between the two different supervisory approaches. The Covered Agreement incorporates, and memorializes, shared mutual respect between the EU and the United States, and will close with finality issues between the United States and the EU that have been pending for more than a decade.

Reinsurance and Group Supervision Issues Resolved with Finality

Neither the United States nor the EU can benefit from the terms of the Covered Agreement without also providing to the other the benefits of the Covered Agreement. In other words, the provisions of the Covered Agreement are cross-conditional. If the United States fails to perform on the reinsurance reforms, then the EU need not comply with the group supervision practices. If the EU does not comply with the group supervision practices, then the United States need not comply with the reinsurance reforms.

The cross-conditional nature of the Covered Agreement incentivizes supervisors in both the EU and the United States to comply with the terms. For this reason, among others, the Covered Agreement does not need to be clarified with further written materials. This would be a fool's errand. The Covered Agreement terms, painstakingly negotiated, are abundantly clear, even if not written to resolve every stakeholder's nuanced fantasies.

To the extent that the EU and the United States have questions about interpretation or implementation in the coming years, the Covered Agreement establishes a Joint Committee to address and resolve any open question. This Joint Committee mechanism, not unlike those established to implement other international agreements, would allow for both broad and targeted subjects to be addressed in a collaborative manner, again a reflection of the shared substantial and mutual benefits of the Covered Agreement.

If both the EU and the United States comply with the Covered Agreement terms, then the Covered Agreement becomes permanent and final. *See* Article 10, paragraph 1.

Federal Insurance Office

After the financial devastation wrought by the financial crisis, and in recognition of the central role of a U.S. insurer in that devastation, Title V of the Dodd-Frank Consumer Protection and Wall Street Reform Act established FIO to complement the work of the states with respect to the U.S. insurance regulatory system.

FIO, an office within Treasury, has statutory authority to represent the United States on prudential aspects of international matters. In doing so, FIO has worked closely with the professionals at the Board of Governors of the Federal Reserve System, state regulators, and staff at the NAIC. By working with our U.S. and international counterparts, FIO built consensus in the development of international standards that incorporates views accommodating the substance and structure of the U.S. insurance regulatory system.

FIO's collaborative domestic and global leadership has served the best interests of U.S. insurance consumers, industry, and the U.S. economy. Make no mistake — U.S. leadership in the global insurance sector is more important and necessary now than at any time before.

This is a time of rapid globalization within the insurance sector as developing economies around the world seek private capital and insurance products to provide the same benefits to their populations that the industry provides in the United States. These are profoundly meaningful opportunities for organic growth for U.S.-based insurers and reinsurers. As each year passes, these reasons for U.S. global engagement and leadership become more obvious and more important.

FIO has afforded the United States insurance sector its most coordinated, forceful and effective global representation. Choosing otherwise puts American interests far in the rear. The debate of whether the U.S. federal government, including FIO, should have a role in U.S. insurance sector oversight is a bygone relic, a debate from another era, and fails to recognize that the U.S. insurance industry, in all of its diversity, deserves prominent U.S. leadership on important global insurance matters. To the extent the debate remains, the actual salient question is whether the United States prefers to lead or to follow.

If the United States does not engage, or lead, then the United States cedes the development of regulatory concepts to other jurisdictions. The global insurance community will not wait for the United States if we repeatedly re-hash the currently unchallenged merits of the McCarran-Ferguson Act.

Further, FIO has played an essential role in domestic oversight of the insurance sector. FIO has published 16 reports, including on topics relating to insurance consumer matters. This work highlights the state-by-state differences and the impact of those differences on the insurance industry and the American people. Industry and consumers have a shared interest in efficient, well-regulated and competitive markets, and FIO's reports on the domestic and global industry should continue to facilitate policymaker analyses.

Too often some posit that the choice between consumer protections and industry interests is binary, a zero sum proposition. FIO's reports, and FIO's engagement on broader domestic issues of insurance public policy, have been premised upon a balanced and factual dialogue that improves insurance sector oversight.

FIO has also engaged domestically in a broad range of matters, including retirement security, resilience to severe weather events, cyber-security, implementation and interpretation of the 2015 terrorism risk insurance program, as well as nuts and bolts insurance projects such as flood insurance and long-term care insurance.

As an industry of $8.5 trillion in assets (2015 total) in the United States, and a critical tool for all aspects of American personal and commercial activity, the insurance industry deserves a prominent place in Treasury, and the U.S. Executive Branch of government. FIO's statutory authorities serve as a perfect complement to the limitations of state regulatory authority. To view FIO differently diminishes the importance the insurance sector in the United States and minimizes the significance of the insurance issues confronting the American people. In other words, without threatening the regulatory role of the states, Federal leadership, including through Congress, will continue to be necessary to address important insurance issues of national and global interest.

Conclusion

Treasury and USTR pursued a Covered Agreement that would memorialize the obvious prerogative of the United States to determine the substance and structure of U.S. insurance oversight. In addition, Treasury and USTR sought a Covered Agreement that would provide meaningful benefits for U.S. insurers, reinsurers, consumers, and for the U.S. economy.

At every point in the Covered Agreement negotiation, Treasury and USTR prioritized the best interests of U.S. consumers, U.S. insurers and the U.S. economy. While providing equally meaningful benefits for the EU, this Covered Agreement achieves every U.S. goal.

Chairman Duffy, Ranking Member Cleaver, thank you for the courtesy and respect that you showed to me throughout my FIO tenure. I valued the chance to work with this Committee and its excellent staff, including your predecessors, and always benefited from our interaction.

Thank you for your attention. I look forward to your questions

Testimony of

Ted Nickel

Commissioner

Office of the Wisconsin Commissioner of Insurance

On Behalf of the National Association of Insurance Commissioners

Before the

Subcommittee on Housing and Insurance

Committee on Financial Services

United States House of Representatives

Regarding:

Assessing the U.S.-EU Covered Agreement

Thank you Chairman Duffy, Ranking Member Cleaver, and members of the subcommittee. My name is Ted Nickel. I serve as insurance commissioner for the state of Wisconsin and current president of the National Association of Insurance Commissioners (NAIC). I greatly appreciate your invitation to testify before you regarding the covered agreement between the European Union and the United States.

The NAIC is committed to working with Congress and the administration to address disparate regulatory treatment some EU jurisdictions are imposing on U.S. insurers doing business in the EU. While a covered agreement is one way to resolve these issues, we oppose this current covered agreement as drafted. We urge Congress and the administration, with direct involvement of states, to expeditiously reopen negotiations with the EU to reach an agreement which brings finality to these issues, and better protects U.S. policyholders, companies, and our state regulatory system.

In September, my colleague Tennessee Insurance Commissioner Julie Mix McPeak outlined for this subcommittee concerns state insurance regulators had with discriminatory actions EU member countries were taking against U.S. firms under the auspices of implementing the EU's new Solvency II regime, lack of necessity for a potentially preemptive covered agreement to resolve concerns relating to those actions, lack of transparency to Congress and stakeholders regarding the nature and progress of the covered agreement negotiations, and lack of meaningful inclusion of state insurance regulators in this process.[1] This agreement, as drafted, does little to resolve those concerns.

While state insurance regulators recognize the U.S. received some limited benefits, this agreement does not provide for full or permanent equivalence or recognition of our time-tested regulatory system, nor does it provide certainty for our U.S. insurance sector. Instead, in a single agreement with an outgoing administration, the EU achieved its primary objective of eliminating U.S. reinsurance collateral requirements designed to protect U.S. consumers. In return, U.S. companies and our regulatory system received only a form of "probation" – limited relief from prescriptive European regulation but under a continued threat where any relief could be revoked if we fail to meet Europe's ongoing expectations and standards. And the burden for this probation is placed almost entirely upon the states, and its underlying costs ultimately will be paid for by U.S. policyholders. My state insurance regulator colleagues and I seriously question whether this agreement meets statutory standards for a covered agreement set forth in the Dodd-Frank Act, which requires such agreement contain measures which are substantially equivalent to the level of protection achieved under state insurance or reinsurance regulation.[2] Indeed, substantive operative provisions of this agreement do not meaningfully address or even reference consumer protection.

Issues addressed by this covered agreement are entirely of the EU's own making (and could be unilaterally resolved by the EU changing its law on equivalence) but they are being solved

[1]United States. Cong. House. Financial Services Subcommittee on Housing and Insurance. *Hearing on the Impact of the U.S.-EU Dialogues on U.S. Insurance Markets*. September 28, 2016. 114th Cong. 2nd sess. Washington: GPO, 2016 (statement of Julie Mix McPeak, Commissioner, Tennessee Department of Commerce and Insurance)

[2] 31 U.S.C. § 313

entirely at the expense of U.S. industry, consumers and regulators. In spite of this imbalance, state regulators are nevertheless unanimously committed to resolving these issues, even if it means a revised federal agreement, so U.S. firms are not put at a competitive disadvantage when operating in the EU. However, as drafted, this covered agreement is not the answer and we urge the Trump administration to reopen negotiations with the EU to obtain a better deal for the United States. State regulators can support an agreement which achieves clear and permanent mutual recognition for our time-tested U.S. insurance regulatory system, includes meaningful state regulator input and transparency in its drafting and execution, and is unambiguous in its terms and finality. This covered agreement fails to meet any of those objectives, and we hope members of Congress will join us in calling for the expeditious reopening of negotiations.

This Agreement Provides Limited Benefit to the U.S. Insurance Sector

As you are aware, on November 20, 2015, the previous administration's Treasury Department and the Office United States Trade Representative (USTR) notified Congress they intended to initiate negotiations to enter into a covered agreement with the European Union.[3] They made it clear they would not enter into a covered agreement unless terms of the agreement were beneficial to the United States and state insurance regulators would have a meaningful role during the covered agreement process. In that notification, the Treasury Department and USTR set out the following negotiating objectives:

1) "treatment of the U.S. insurance regulatory system by the EU as 'equivalent'" under Solvency II "to allow for a level playing field for U.S insurers and reinsurers operating in the EU;"
2) "recognition" by the EU of the U.S. insurance regulatory system, including with respect to group supervision;
3) "Facilitat[ion of the] the exchange of confidential regulatory information between lead supervisors across national borders;"[4]
4) "nationally uniform treatment of EU-based reinsurers operating in the United States, including with respect to collateral requirements;" and
5) "permanent equivalent treatment of the solvency regime in the United States and applicable to insurance and reinsurance undertakings."

The previous administration failed to meet several of these objectives. While we recognize the agreement appears to provide some benefit to U.S. insurers operating in the EU by eliminating EU local presence requirements over time, this agreement does not require the EU to grant the U.S. permanent equivalence (or comparable treatment), and in fact, the word "equivalence" is nowhere to be found in the document. This means, even post covered agreement, insurers based in Bermuda or Switzerland, for example, (which have received equivalence) receive greater benefits from the EU than U.S. insurers. So even under this agreement, the United States, one of the most sophisticated and well-regulated insurance marketplaces on the globe, continues to be

[3] Wall, Anne. Harney, Michael. Letter to Congress Re: Initiation of Covered Agreement Negotiations, 20 Nov. 2015.
[4] The agreement encourages, but does not require, supervisory authorities to cooperate in exchanging information while respecting a high standard of confidentiality protection. It appears to do little of substance in relation to laws or procedures related to information exchange.

treated by Europe as a parolee. We remain under suspicion, we continue to be monitored, and whatever freedoms afforded by this agreement can be revoked.

Similarly, this agreement also fails to grant full "recognition" by the EU of the U.S. insurance regulatory system, including with respect to group supervision. While this agreement appears to prevent the EU from imposing its requirements on the "worldwide parent" located in the United States, it does not provide promised "recognition" or require the EU to recognize the U.S. as equivalent. Further, the language is ambiguous as to the obligations of the parties and the entities to which it applies (e.g., the insurance group, the insurance and non-insurance group, the legal entities, or a combination). Troubling, this agreement also places conditions on the ability of regulators to obtain information or take certain actions currently authorized under state laws. Indeed, there are potential conflicts between provisions and limitations in this agreement and existing state reporting processes as well as critical examination and hazardous financial condition authority.

In addition, many key terms describing the circumstances which would prompt action by regulators to comply with this agreement are undefined or ambiguous. For example, the agreement acknowledges a need for a group capital requirement or assessment, but it also requires "the authority to impose preventive, corrective, or otherwise responsive measures on the basis of the assessment, including requiring, where appropriate, capital measures."[5] The provision implies state insurance regulators are effectively required to develop and adopt a group capital requirement but also includes language suggesting the EU could apply its own group capital requirements and re-impose local presence requirements if states choose not to act. In other words, this agreement seems to compel states to subject a broad group of insurers to additional regulation with no guarantee the EU ultimately would not apply its own layer of requirements if it finds the additional U.S. approach to be unsatisfactory.

This agreement is littered with ambiguities such as these and they would have to be resolved by an undefined "Joint Committee" composed of representatives of the U.S. and EU. This agreement does not set forth how many representatives will compose the Joint Committee or indicate which persons or bodies will be represented. Importantly, there is no mention of a role for state insurance regulators, who are charged with implementing much of this agreement and whose laws and regulations may be directly impacted or preempted. We are already aware of agreement provisions the U.S. and EU negotiators interpret differently. If a meeting of the minds cannot be reached on these ambiguities, this agreement may be voided —under its terms, if any single provision of this agreement is violated, the other party is not obligated to follow other provisions of this agreement. This framework inevitably will lead to perpetual renegotiations through the Joint Committee and uncertainty for U.S. industry, policyholders, and regulators.

The one objective met was a key negotiating priority for the EU, elimination of reinsurance collateral requirements. In fairness, this covered agreement retains a few of the elements from the NAIC's Credit for Reinsurance model laws, including requirements with respect to enforcement of final U.S. judgments, service of process, financial reporting requirements, prompt payment of claims, and solvent schemes of arrangement. These requirements are also

[5] *Bilateral Agreement between the European Union and the United States of America on Prudential Measures Regarding Insurance and Reinsurance*, January 13, 2017, p. 12.

applicable to U.S. reinsurers doing business in the EU, and collateral may be imposed if these requirements are not met under a process established in this agreement. However, this agreement does not include any evaluation of reinsurer creditworthiness and despite the Treasury Department having verbally committed it would never accept an agreement which eliminates reinsurance collateral, it did exactly that.

Collateral is not just some illusory consumer protection. Reinsurance capital moves quickly worldwide in search of attractive returns. It is important; as we have seen when catastrophes strike, to have solid assurances that claims will be paid immediately. Existence of collateral provides strong incentives for reinsurers to perform on their obligations and regulatory requirements to protect all insurers, particularly smaller insurers who may not have the leverage to renegotiate and require it contractually from reinsurers with whom they do business. Even though the probability of failure may be low, particularly for large, financially sound, international reinsurers, the impact of failure could be catastrophic to U.S. ceding insurers and policyholders in the absence of collateral as a safety net. It is understandable some may argue financially strong reinsurers should not have to post collateral, but many non-U.S. reinsurers who failed (e.g., Gerling, Trenwick, Legion) were considered paragons of strength only a few years before their collapse.[6]

Though we believe it is necessary for counterparties to have "skin in the game" (a lesson the financial system was reminded of during the financial crisis with respect to other financial instruments), we have nevertheless attempted to be responsive to the European insurance industry and governments who have sought reduction of such requirements. We have worked tirelessly to reduce collateral requirements by amending NAIC's Credit for Reinsurance Model Act to allow for reduction in collateral based on the strength of the insurer and its regulatory regime. The amendments have already been adopted by 35 states representing approximately 69 percent of direct written premium and will become an accreditation requirement on January 1, 2019, leading to further adoption by states. In fact, based on these changes, the amount of collateral posted by EU reinsurers has dropped dramatically. In 2015, EU-based reinsurers posted only \$31.4 billion or 15.4 percent of the almost \$205 billion in collateral posted worldwide, but when you consider collateral represents significantly larger commitments to U.S. policyholders, retaining some collateral is a reasonable approach. While we are open to further discussions on collateral reduction and even changes to our present credit for reinsurance construct, wholesale elimination of this regulatory requirement to benefit foreign reinsurers should be weighed more thoughtfully against potential harm to U.S. companies and consumers. With absence of collateral, regulators will have to find other mechanisms with which to protect insurers and their policyholders from the risks posed by counterparties such as reinsurers possibly including new capital charges or restrictions imposed on ceding insurers. This covered agreement will essentially transfer credit risk of foreign reinsurers to their customers: U.S. insurance companies, and by extension, U.S. policyholders.

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[6] *U.S. Reinsurance Collateral*, NAIC Reinsurance Task Force of the Financial Condition (E) Committee, March 5, 2006, p. 19.

The Process was Flawed

The poor results achieved during this negotiation are not surprising because the process was flawed from the outset. Following notification to Congress, the Treasury Department and USTR negotiated for over a year behind closed doors. Unlike a trade agreement, which is subject to established procedures for consultation and input from the states and a vote by the Congress, there was no formal consultation with a broader group of U.S. stakeholders including industry and consumer participants. State regulators were assured we would have direct and meaningful participation in this covered agreement process, but the small group of us included in the process were merely observers, only one allowed in the room at a time, subject to strict confidentiality with no ability to consult our staff and fellow regulators. This agreement was finalized in the waning days of the previous administration and announced on January 13, 2017—a week after the former Federal Insurance Office director had announced his resignation effective January 20th. The process was also skewed in favor of the EU from the beginning by the fact that it retained the ability to approve the agreement by the European Parliament and the European Council, whereas the U.S. retained virtually no congressional vetting authority prior to possible preemption of U.S. insurance regulations.

This was a flawed process which produced a flawed document. Instead of an agreement negotiated by subject matter experts from the U.S. accountable to the consumers and markets they represent, we have an agreement mostly negotiated by Treasury bureaucrats in the waning days of an outgoing administration. This agreement sets a precedent others around the world may try to imitate and, put in the simplest terms, forces U.S. acquiescence which weakens our standards in exchange for very little. Treasury and USTR stated they would not enter into a covered agreement unless the terms were beneficial to the U.S. They failed to meet that objective.

A Path Forward

Notwithstanding this specific agreement does not sufficiently benefit the U.S insurance sector, state insurance regulators remain committed to working with the administration, EU, Congress, and stakeholders to negotiate one which does. We would like the administration to expeditiously establish a negotiation process which is more transparent, allows for more robust congressional and stakeholder engagement, and provides actual meaningful and direct participation by insurance regulators including the ability for all impacted regulators to review terms as they develop. States are the primary regulators of the insurance sector and would have to implement provisions of any agreement. Our involvement and buy-in is essential to its success. In terms of specific substantive improvements, we would expect any agreement to provide for permanent mutual recognition, equivalence, or comparable treatment for U.S. firms operating in the EU, full recognition of the U.S regulatory system and its approaches to group supervision and capital, clarity in the agreement's terms, and finality in its application. We recognize that the EU would have expectations regarding collateral and state insurance regulators would be open to making further changes to our credit for reinsurance laws to address those demands, but any approach we would seek would remain risk-based to ensure U.S. insurers and policyholders were adequately protected.

Conclusion

We are aware this agreement has its proponents, but we should not confuse any deal with a truly beneficial deal, and we perceive benefits of this agreement to be fleeting and illusory. Our request to renegotiate is not made lightly, or a case of making the perfect the enemy of the good. A renegotiation of this agreement using a better, more transparent process led by an administration which is not in its final days, with full participation of insurance regulators will lead to a better result for the United States. Working together with this current administration and Congress, we believe we can achieve the finality, certainty, and recognition lacking in this current agreement without sacrificing key consumer protections. Thank you for this opportunity to testify today and I would be pleased to take your questions.

Testimony of

Leigh Ann Pusey, President and CEO
American Insurance Association

Before the House Financial Services Committee
Subcommittee on Housing and Insurance

Hearing entitled "Assessing the U.S. – EU Covered Agreement"
February 16, 2017

Chairman Duffy, Ranking Member Cleaver, Members of the Subcommittee, thank you for the opportunity to testify on behalf of the American Insurance Association (AIA) to provide our assessment of the Covered Agreement entered into by the United States (U.S.) and the European Union (EU).

Celebrating its 150th year in 2016, AIA is the leading U.S. property-casualty insurance trade organization, representing approximately 320 insurers that write more than $125 billion in U.S. property-casualty premiums each year. AIA member companies offer all types of property - casualty insurance, including personal and commercial auto insurance, commercial property and liability coverage, specialty, workers' compensation, homeowners' insurance, medical malpractice coverage, and product liability insurance. AIA's membership includes U.S. insurers that write insurance only within the U.S., U.S. insurers that write insurance inside and outside the U.S. (including in the EU), and the U.S. subsidiaries of multi-national insurers. This membership diversity gives AIA the ability to analyze issues from many perspectives and enables us to draw on the global experience and expertise of our companies with many forms of insurance regulation.

AIA believes that the new international agreement on insurance and reinsurance prudential measures is a win for industry and for the U.S. system of insurance regulation. It gives international recognition to the state-based insurance regulatory system and provides U.S. insurers and reinsurers the badly-needed certainty that they will no longer face discriminatory regulatory measures in the EU. Equally important, it sets a valuable precedent that will protect the state regulatory system from future attempts to import inconsistent or conflicting international regulatory standards.

The U.S. Treasury's Federal Insurance Office (FIO) and the U.S. Trade Representative (USTR) announced in November 2015 that they would enter into negotiations for a "Covered Agreement" on insurance prudential matters with the EU. On January 13, 2017, they revealed that those negotiations were complete, and submitted the Agreement to Congress. U.S. state insurance commissioners played a significant role advising the U.S. negotiators every step of the way, and through their efforts, the agreement affirms our state-based system of regulating insurance, incorporating key aspects of existing NAIC models and state provisions along the way.

The deal could not have come too soon. Since the EU's Solvency II Directive was activated on January 1, 2016, U.S. (re)insurance groups that do business in the EU have faced increasingly discriminatory regulations from EU Member State governments. Unnecessary regulatory divergence between the U.S. and EU quickly turned into market access barriers as U.S.-based reinsurers were told they could not offer reinsurance in the EU, and U.S. insurance groups were threatened with onerous, duplicative regulatory requirements arising from their operations in the EU.

By upholding the U.S. system of state-based insurance regulation, the Covered Agreement will re-establish a level playing field for U.S. insurers and reinsurers competing in the EU, requiring regulatory treatment of U.S. groups in the EU to be no less favorable than the treatment received by EU (re)insurers. Specifically, the Covered Agreement limits "global" group supervision to the home country supervisor, meaning U.S. insurers operating in the EU will be subject to applicable worldwide prudential insurance group oversight only by their home U.S. supervisor. In addition, it guarantees that EU regulators will no longer tell U.S. reinsurers that they have to establish a local presence in each EU country to do business there. In this way, the Agreement fosters a climate of reciprocal regulatory respect in the EU and the U.S., which will lead to a better operating environment in the world's two largest insurance markets.

The recognition afforded to the U.S. state-based system is also a victory for U.S. consumers and policyholders. Allowing market access to more companies under the Agreement's conditions – both in the U.S. and the EU – improves consumer choice and expands insurance and reinsurance availability. Equally important, our regulatory system is predicated on policyholder protection and, through the Covered Agreement, the EU is explicitly acknowledging the value of that approach for those insurance and reinsurance groups that call the U.S. home.

Additionally, the Covered Agreement is an alternative to submitting to the EU's "equivalence" process - a European legal process that provides benefits to insurance and reinsurance groups from countries that are willing to model their regulatory frameworks on the EU's Solvency II Directive. Rather than requiring significant changes to the U.S. state regulatory architecture, the Covered Agreement allows regulators on both sides to rely on the existing structure in each other's jurisdictions while at the same time providing the fair treatment guaranteed to "equivalent" jurisdictions.

It is important to note that it was the view of U.S. negotiators, including U.S. state insurance commissioners, not to enter into the EU's Solvency II "equivalency" process. On July 11, 2014, state insurance commissioners wrote to the European Commission confirming that the U.S. was not pursuing "equivalence," citing the significant changes to the U.S. supervisory system that such a path would entail and instead encouraging the Commission to reach an alternative "similar conclusion about the efficacy of our system."[1]

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[1]Letter from NAIC International Relations Leadership Group to Jonathan Faull (Director General, European Commission) at p. 1 (July 11, 2014) ("As you know, U.S. state insurance regulators are not pursuing an equivalence determination. While it is possible to compare our respective statutory authorities on paper, it would be

Because of the Covered Agreement, the states preserve the current system without compliance with the burdensome Solvency II requirements for group global capital, reporting, and corporate governance. Indeed, in order to complete the "equivalence" process, U.S. supervisors would have had to develop a global group capital requirement that is similar in substance to the EU directive, rather than the group capital calculation initiative that is under development at the NAIC.

Moreover, many of the provisions in the group supervision and reinsurance sections are drawn directly from state law and state insurance commissioners' models promulgated by the NAIC, including (as noted) the current efforts of U.S. state insurance regulators in developing a group capital assessment and reducing statutory reinsurance collateral requirements. Importantly, per the scope of the Agreement, it also covers only those U.S. (re)insurance groups that have EU operations and, by extension, only those states that supervise those U.S. groups.

For "global" group capital in the U.S., the Agreement effectively accepts a group assessment or calculation as long as that assessment or calculation captures risk of the entire group (limited to insurance entities or those entities controlled by an insurance entity) and, consistent with current U.S. state law, the supervisor has the authority to take appropriate measures on the basis of the assessment. The Covered Agreement does not specify that the authority must extend to the entire group, however, and does not dictate what constitutes appropriate measures.

In fact, the NAIC is currently in the process of developing a group capital calculation, which it calls the "inventory method." The inventory method leverages the U.S. risk-based capital (RBC) approach to assess group capital through an aggregation of legal entity capital requirements. That method is envisioned as a tool that can be used by state regulators in the supervisory college context to better assess the capital adequacy of a U.S. group's global insurance operations, and meets the conditions outlined in the Covered Agreement.

The Covered Agreement also addresses the issue of reinsurance collateral. As stated in the Treasury Department's Fact Sheet, the Covered Agreement "eliminates collateral and local presence requirements for U.S. reinsurers operating in the EU insurance market, and eliminates collateral and local presence requirements for EU reinsurers operating in the U.S. insurance market, as a condition for and in connection with regulatory credit for reinsurance." As mentioned earlier, this provision guarantees that EU regulators will no longer tell U.S. reinsurers that they have to undergo the expense and duplication of opening local offices in each EU member state, in order to do business there.

Although the Agreement, consistent with existing language in Title V of Dodd-Frank, does allow for a very narrow preemption process to accommodate for non-discriminatory state reinsurance law practices, it is not clear that the preemption process will need to be used at all. The Covered Agreement recognizes and utilizes the work done by the NAIC during the development of its model on credit for reinsurance. Over the past several years, 35 states have already begun reducing the levels of statutory reinsurance collateral requirements through

challenging to conduct a comprehensive comparison of our two regulatory systems in practice until Solvency 2 is fully operational and the outcomes it produces based on actual experience are better understood.")

adoption of the NAIC's model law from 100 percent to between ten and twenty percent. Ultimately, each affected state will have 5 years to put in place those tools and provisions that effectuate the reinsurance and group supervision articles of the Agreement. If anything, those states have a head start because of the ongoing work on both issues fostered by the NAIC and individual state insurance commissioners. In addition, the NAIC has declared the credit for reinsurance model to be an accreditation standard on January 1, 2019, which will prompt the states to enact laws that will assure their accredited status well. It is our belief that without a provision to bring parity to the U.S. and EU (re)insurance markets, an agreement to recognize the U.S. state-based system for prudential regulation could not have been reached.

However, as mentioned, the Agreement retains many protections that allow for states and insurers to maintain healthy and well-functioning reinsurance markets in their respective jurisdictions. First and foremost, the Covered Agreement explicitly acknowledges that contracting parties will continue to be able to negotiate for appropriate levels of reinsurance collateral as part of those reinsurance contracts. The Agreement also confirms that the new collateral requirements are to be applied prospectively to new contracts, borrowing language that was part of a unanimously adopted NAIC credit for reinsurance model. Moreover, the benefits of the Agreement only apply to EU reinsurers meeting certain capital and surplus requirements and who have a history of prompt payment of reinsurance claims and comply with financial statement filing requirements – conditions that, again, produced state regulatory consensus in developing the NAIC credit for reinsurance model. As discouragement against bad actors, the states also maintain the ability to require prompt payment of reinsurance claims. And should an EU reinsurer resist a state's final judgment of payment, the state will be able to require 100 percent collateral for all of that reinsurer's liabilities in the state.

Having completed the first successful Covered Agreement negotiation, we now have the opportunity to reflect on both the product and the process. Given the fearful rhetoric that a Covered Agreement could become a back door to import broad swaths of European-style regulation, the Covered Agreement is ultimately proving to be a narrow, focused vehicle that compels the EU to recognize and respect the U.S. state-based system of insurance supervision. In fact, the Covered Agreement is proof that issues regarding prudential matters can be addressed while respecting local regulatory regimes. Importantly, the Covered Agreement advances the competitiveness of U.S. companies in the EU by providing a useful tool to resolve an international issue that was not originally foreseen when the Covered Agreement was conceived.

While improvements can be made to the negotiating process going forward, AIA hopes that this Agreement can continue to be evaluated on its merits. Process should always be scrutinized so that it works for all stakeholders in the future. For our part, AIA consistently advocated for a significant role for U.S. state regulators. And in a development that was unprecedented in U.S. Government international negotiations, our understanding is that a group of state insurance commissioners, chosen by their peers, was given an official consultative role in the process; were provided access to negotiating texts from the EU and the opportunity to comment on all such texts and U.S. proposals before they were presented to the EU negotiators; and were able to view all proposals from the EU.

However, anything that can be done to increase transparency and stakeholder involvement while maintaining the integrity of negotiations should be on the table. In fact, in an attempt to foster better communication, transparency, and uniformity, AIA has recently unveiled a proposal to formalize state insurance regulator involvement in future negotiations by creating a State Insurance Regulator Advisory Board that would coordinate with FIO. By facilitating an on-going, dedicated line of consultation between the states and FIO, state insurance regulators can better inform U.S. negotiators on critical insurance issues in advance of potential future international negotiations, as well as provide informed views for the development of other insurance-related policy matters at the federal level.

In response to the question of whether the Covered Agreement could create any unintended consequences for consumers, policyholders, or segments of the insurance industry, AIA does not believe that this is the case. To the extent that the Agreement follows (or, in some cases, builds upon) strong conditions in the NAIC model, the process of statutory collateral reduction has been anticipated and is underway already. Moreover, the increased levels of capital and the greater regulatory certainty of global reinsurance markets should create more competition among reinsurers and positive market effects, which could help offset any potential adverse effects for small insurers.

In the area of group supervision – and, more specifically, group capital – the Covered Agreement reinforces state regulation without importing inconsistent Solvency II measures and leverages ongoing initiatives launched by the NAIC. Equally important, the Agreement can be used as evidence that significant insurance markets can resolve international prudential issues without perpetuating unfair regulatory discrimination or forcing the adoption of rigid and unworkable standards. For example, in the debate surrounding the International Association of Insurance Supervisors' (IAIS) development of a global insurance group capital standard (ICS), AIA has repeatedly stated that the ICS should be constructed in a manner that respects local regulatory regimes, including the U.S. state-based RBC system. More than 2 years ago, we respectfully suggested that the IAIS allow flexibility to consider and incorporate an aggregation approach that is an early version of the inventory method being discussed by the NAIC and the building blocks approach proposed by the U.S. Federal Reserve Board. At the time, our suggestion was met with deafening silence, as the ICS process moved forward on a technical path. Perhaps the Covered Agreement will be a model for civil discussion on, and resolution of, this and other global supervisory initiatives.

In conclusion, the completion of the Covered Agreement is a success for U.S. insurers and the U.S. regulatory system. It is also a crucial step forward in addressing the modern issues that face global insurance markets. With support, its benefits for insurers and policyholders can continue to grow. Without support, those benefits will be threatened, and we will return to a climate of mutual distrust.

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American Agricultural Insurance Company
Providing Reinsurance Since 1948

February 15, 2017

The Honorable Sean Duffy
Chair, House Financial Services Committee, Subcommittee on
Housing and Insurance
2330 Rayburn House Office Building
Washington, DC 20515

Dear Mr. Duffy:

I understand that on Thursday, February 16, 2017, you will hold a subcommittee hearing on "Assessing the U.S. - EU Covered Agreement," pertaining to a Bilateral Agreement between the European Union and the United States of America on Prudential Measures Regarding Insurance and Reinsurance ("Covered Agreement"). On behalf of American Agricultural Insurance Company ("AAIC"), I wish to voice strong support for the Covered Agreement.

AAIC is an Indiana domiciled company that was incorporated on May 18, 1948. With over a billion dollars in invested assets, AAIC's principal business is reinsurance. The company has over a hundred employees located in two locations: Schaumburg, Illinois, and Columbus, Ohio. Since 1999, AAIC has followed a strategic plan to grow and diversify its reinsurance business by serving as an assuming reinsurer in certain international markets. In turn, AAIC participates in reinsurance transactions throughout the world with 26.5% of its international assumed reinsurance business conducted with insurance companies located in countries in the European Union.

Regulatory changes, including the European Union's adoption of Solvency II, have placed AAIC at a competitive disadvantage in its attempts to gain (or even, at times, maintain) market share in European Union countries. For example, BaFin (the insurance regulator in Germany) has made it clear that AAIC (and other similarly situated companies) cannot reinsure German companies unless it establishes a physical branch in Germany. This type of regulation inhibits growth and can be prohibitively expensive. Similarly, the Belgium, Netherlands and Polish insurance regulators recently placed restrictions on non-EU companies seeking to reinsure companies in their respective countries. AAIC took steps to maintain long standing business relationships with companies in the European Union, but such steps were costly and do not promote the development of long-standing relationships based upon years of information sharing and joint development of risk transfer solutions. In fact, AAIC recently lost business with eight European Union based insurance companies, and I fear that it will be very hard to recapture (or replace) that business unless the regulatory dynamic is altered to level the playing field. In the end, like so many businesses, the business of reinsurance is built on trust and long-term relationships, and a failure to address the regulatory challenges facing AAIC and other similar situated U.S. based companies would be a mistake.

The Covered Agreement is an effective and immediate answer for AAIC and other U.S. based reinsurance companies by: (1) allowing AAIC an immediate opportunity to repair and rebuild damaged relationships in the European Union; (2) providing AAIC a path to equal footing in the international reinsurance marketplace unencumbered by challenging regulatory burdens not faced by its competitors; and (3) facilitating the transfer of insurance and reinsurance risk through a system that benefits companies and consumers around the globe.

I urge your subcommittee to allow the Covered Agreement to remain in effect for the benefit of AAIC, its employees and similarly situated U.S. reinsurance companies.

Sincerely,

AMERICAN AGRICULTURAL INSURANCE COMPANY

Janet S. Katz
Executive Vice President and Chief Executive Officer

ACLI
Financial Security...for Life.

Hearing Statement of the Honorable Dirk Kempthorne
President and Chief Executive Officer
The American Council of Life Insurers
Before the
U.S. House of Representatives Committee on Financial Services
Subcommittee on Housing and Insurance

"Assessing the U.S.-EU Covered Agreement"

February 16, 2017

On behalf of the American Council of Life Insurers (ACLI), I am pleased to submit this statement for the hearing record in support of the U.S.-EU covered agreement. We thank Chairman Sean P. Duffy (R-WI) and Ranking Member Emanuel Cleaver (D-MO) for holding this important hearing. ACLI supports the covered agreement because it strengthens U.S. competitiveness. In the negotiation of the covered agreement, we supported participation of state insurance regulators. We look forward to their active involvement in its implementation and administration.

The ACLI is a Washington, D.C.-based trade association with approximately 290 member companies operating in the United States and abroad. ACLI advocates in state, federal, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing 94 percent of industry assets, 93 percent of life insurance premiums, and 97 percent of annuity considerations in the United States.

ACLI Supports the Covered Agreement.

The covered agreement will make U.S.-based insurers and reinsurers more competitive. It respects our state-based system of insurance regulation. It facilitates and encourages coordination and cooperation between U.S. insurance regulators and EU insurance supervisors, which reduces regulatory burdens for the insurance industry on both sides of the Atlantic. It maintains protections for U.S. insurers that buy reinsurance from EU-based reinsurers. It preserves the sovereignty of our U.S. regulators to impose corrective measures on an EU-based reinsurer if it fails to respect any judgment. It also preserves U.S.

regulators' authority to impose corrective measures on any EU-based insurer if its financial condition threatens policyholder protection or financial stability.

The Covered Agreement Makes U.S.-Based Insurers and Reinsurers More Competitive, Now.

The covered agreement was negotiated to provide significant immediate benefits to U.S.-based insurers and reinsurers. With this agreement, EU supervisors will not require U.S.-based insurers to be subject to global group reporting, governance, or capital requirements. That represents significant savings to U.S.-based insurers doing business in EU member states.

U.S.-based reinsurers also benefit immediately because the EU will allow them to sell reinsurance cross-border now, with this agreement, without requiring a local presence. It has also agreed to change its laws within 24 months to permit U.S.-based reinsurers to sell reinsurance cross-border. The agreement says that if the EU fails to change its laws within that time, then the United States can impose global group capital requirements on EU insurers doing business in the United States. That pledge by the EU is very valuable to U.S.-based reinsurers doing business in any EU member country.

U.S.-based insurers and reinsurers also benefit from the predictability that the covered agreement gives to those doing business in EU member states. Before the agreement, each EU member state could impose its own requirements on U.S.-based insurers doing business in that country. That lack of predictability and certainty caused much concern and expense since Solvency II came into effect January 1, 2016. ACLI members will benefit from the predictability and certainty that the covered agreement brings to EU member states' implementation of Solvency II. That predictability and certainty will promote their competitiveness.

The Agreement Respects Current State-Based Insurance Regulation.

The covered agreement specifically states its respect for our system of state-based insurance regulation. It also demonstrates that respect by:

Deferring to the current state-based method of group supervision and policyholder protection;

Recognizing the states' existing authorities to implement remedial and corrective measures; and

Promoting the uniform application of the NAIC Credit for Reinsurance Model Law and Regulation.

Both EU and U.S. negotiators have affirmed that the agreement was not intended to and does not require any change to the current U.S. system of insurance group supervision.

This is a critical point. The EU has accepted the current U.S. system of indirect group supervision.

The Agreement Provides Reinsurance Collateral Parity.

U.S. insurance regulators have worked diligently for many years to reduce collateral required of reinsurers based in other countries and doing business in the United States. In 2011, the NAIC unanimously adopted a model law and accompanying regulation that allowed collateral to be reduced to zero (for very solvent reinsurers from well regulated countries) from the 100% level that had historically been required of all reinsurers. Thirty-five states have adopted the model law; twenty-five states have adopted the regulation.

Some EU member states have nonetheless maintained collateral requirements for U.S.-based 'foreign' reinsurers doing business in that country. The covered agreement assures that U.S. reduction in collateral is not unilateral—requiring that all EU member states reduce collateral to zero on the same timetable for very solvent U.S.-based reinsurers. This will make U.S.-based reinsurers more competitive.

The Agreement Preserves Protections for U.S. Insurers and Policyholders.

The NAIC model law and regulation on credit for reinsurance contain many protections for U.S. insurers and policyholders. The covered agreement maintains these protections, including state regulators' authority to require any reinsurer to submit to its authority, report on its financial condition and its payment practices, pay any final judgements, and post collateral retroactively. The agreement does not compromise state insurance regulators' authority to protect U.S. insurers and U.S. policyholders.

Any Preemption Is Remote and May Not Be Necessary.

ACLI supports the U.S. system of state-based insurance regulation. ACLI supports the Dodd-Frank Act's restrictions on the authority of the Federal Insurance Office to act generally as a regulator. ACLI supports the Act's strict limitations on preemption and its cautious and deliberative approach to any discussion of preemption. These Dodd-Frank Act provisions preserve the primacy of our national system of state-based insurance regulation.

There is no question of any preemption with respect to the covered agreement's text on group supervision or on the supervisory exchange of confidential information. The EU has accepted the U.S. approach to group supervision, and U.S. regulators and EU supervisors agree on how to exchange non-public supervisory information.

The covered agreement does raise the possibility of preemption in its text on reinsurance collateral. We believe that possibility is quite limited, if not remote. The NAIC has established its model law and regulation on credit for reinsurance as an accreditation standard as of January 2019, meaning that state regulation is well-positioned to implement any revisions.

The Dodd-Frank Act has substantial protections against any preemption. No preemption is allowed unless the state requirement treats non-U.S. insurers less favorably than U.S. insurers licensed in that state. The new requirement must provide a substantially equivalent level of protection for consumers. The Act also has substantial process protections. The federal government must consult with the state and the public and consider their input before any preemption. The federal government must also notify the committees of jurisdiction in Congress upon any preemption. Finally, the Act allows de novo judicial review of any preemption.

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ACLI believes that the benefits of the covered agreement to the competitiveness of the U.S. insurance industry and to state regulation are immediate and substantial. We urge Members of Congress to support it.

Again, ACLI appreciates the opportunity to offer this statement in support of the U.S.-EU covered agreement.

Sincerely,

GOVERNOR DIRK KEMPTHORNE

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February 15, 2017

The Honorable Sean P. Duffy
Chairman
Subcommittee on Housing and Insurance
Financial Services Committee
U.S. House of Representatives
Washington, DC 20515

The Honorable Emmanuel Cleaver
Ranking Member
Subcommittee on Housing and Insurance
Financial Services Committee
U.S. House of Representatives
Washington, DC 20515

CHUBB

Dear Chairman Duffy and Ranking Member Cleaver:

In anticipation of the February 16, 2017 Subcommittee hearing entitled "Assessing the U.S.-EU Covered Agreement," Chubb would like to submit this letter for the record.

Chubb is the world's largest publicly traded property and casualty insurer. We employee over 16,500 people in the United States. The U.S. accounts for over 60% of Chubb's premium written, while Europe accounts for an additional 14%. We believe a healthy, mutually beneficial relationship between the U.S. and EU is in our national interest and is clearly in our company's interest. Together, the U.S. and EU account for nearly 70% of total global insurance premiums written. Allowing for a mutually beneficial insurance market relationship between the U.S. and EU benefits consumers by providing greater product choice and affordability.

Chubb is a strong supporter of the U.S. state-based insurance regulatory system. It is a system that has proven to be effective for over a century. We believe the Covered Agreement is a tool that helps preserve this system. The Agreement affirms the U.S. system of insurance regulation, including the role of state insurance regulators as the primary supervisors of the business of insurance.

Solvency II, the EU's regulatory system which went into effect last January, has created barriers to U.S. companies operating in Europe. The Covered Agreement helps alleviate those problems. As an example, our European operations are conducted through our United Kingdom based subsidiary. Our global group supervisor is the state of Pennsylvania. However, we were informed by the U.K. Prudential Regulatory Authority (PRA) that they would apply Solvency II prudential measures to our global operations, including group capital requirements, governance and reporting since we were regulated by a "non-equivalent" authority. While the PRA instituted a waiver process, it is still duplicative, burdensome, costly and temporary. Our waiver expires in December 2018, at which point we would need to go through the waiver process again. Higher costs and capital requirements associated with Solvency II would dampen our ability to offer products to our customers around the world.

Various EU Member States have also demanded that U.S. reinsurers establish a local presence in their countries given that the U.S. is "non-equivalent." These actions have adversely impacted U.S. reinsurers operating in Europe. We believe inhibiting the availability of reinsurance is detrimental to Europe and the U.S. given the importance of spreading risk globally.

The Covered Agreement has addressed these concerns in an effective manner. Instead of kowtowing to the European system of regulation, the Covered Agreement affirms our state-based system and makes it more difficult for the EU to globally proselytize about Solvency II as the only appropriate regulatory system.

On group supervision, the Covered Agreement limits the worldwide application of Solvency II on U.S. insurers operating in Europe. The group supervision provisions only apply to U.S. insurers operating in Europe. This allows for Pennsylvania to remain as our sole global group supervisor.

The Covered Agreement eliminates collateral and local presence requirements for U.S. insurers operating in the EU market and provides reciprocal access to EU insurers in the U.S. This builds on the reinsurance collateral reform that state regulators initiated in 2011. The agreement on reinsurance is beneficial bilaterally, but globally as well. By affirming that both the U.S. and Europe judge reinsurers by their merits and not by their geography, the Covered Agreement sends a strong signal supporting open trade in a sector that is premised on global risk diversification. U.S. (re)insurers are facing increasing regulations in many developing markets aimed at protecting local (re)insurers to the detriment of U.S. firms.

No agreement is perfect. Given our state-based system of regulation, we would have supported a greater role for state regulators in the negotiating process and hope that state regulators will have a significant role in the Joint Committee established through the Covered Agreement.

Without the Covered Agreement, the irritants noted above would remain. This would likely lead to a further deterioration in U.S.-EU relations, and increased impediments to market access, directly hurting consumers. The Agreement entrusts both parties to take steps over a period of years. This will require monitoring by Congress, regulators and the insurance sector. We look forward to supporting the mutually beneficial implementation of the agreement.

Sincerely,

Trish Henry

Patricia A. Henry

Global Government Affairs Officer

VIEWS OF THE CINCINNATI INSURANCE COMPANIES ON COVERED AGREEMENTS

Statement for the Record Prepared for the House Financial Services Housing & Insurance Subcommittee Hearing on "Assessing the U.S.-EU Covered Agreement"

[February 16, 2017]

THE U.S. SHOULD RENEGOTIATE THE PENDING COVERED AGREEMENT. The pending covered agreement should be pulled back and renegotiated since the process under which it was negotiated failed on many levels and resulted in an agreement with many procedural and substantive flaws, the terms of which could greatly damage the primacy of our state insurance regulatory system.

LACK OF TRANSPARENCY IN THE PROCESS. There was no transparency in the negotiation process. During the negotiation process there were no meaningful stakeholder process or updates for the public on the substance of what was being negotiated, and the text of the agreement was hidden from the public until it was filed with Congress on January 13, 2017.

STATE REGULATORS BARRED FROM THE NEGOTIATING TABLE. The law governing the covered agreement negotiations prohibited any meaningful participation by state regulators. State regulators were allowed to attend the negotiating sessions but were not permitted to directly or actively negotiate and were forced to sign nondisclosure agreements preventing them from revealing what they heard in those sessions. Had state regulators had real negotiating power, the outcome of the negotiation would have almost certainly been different and the terms of the covered agreement better. Instead, state regulators were put in the terrible position of being forced to watch on the sidelines as the Administration and a foreign power reshaped the landscape of state insurance regulation on reissuance collateral and group capital requirements.

THERE WAS NO NEED TO ADDRESS REINSURANCE COLLATERAL IN THE COVERED AGREEMENT. Had state regulators been allowed a meaningful role in the negotiations of the covered agreement, they would have most certainly argued against including the "zero reinsurance collateral" preemption provision in the covered agreement since the U.S. already has a state-regulated system that allows EU reinsurers to post zero collateral in the U.S. if they achieve the "Secure—1" financial strength rating under the NAIC's "sliding scale" reinsurance collateral model law. The NAIC model is well on its way to being adopted in all 50 states; 35 states have already enacted the model law and the pace for adoption by the rest of the states will now quicken since the NAIC has made enactment of the model law an accreditation requirement.[1]

THE NAIC'S "SLIDING SCALE" COLLATERAL LAW IS BETTER FOR CONSUMERS. The NAIC's "sliding scale" reinsurance collateral law is better for consumers than the provision included in the covered agreement since the NAIC model provides six different financial strength rating categories for EU reinsurers; the reinsurance collateral provision in the covered agreement only utilizes one financial strength rating for EU reinsurers. Under the NAIC sliding scale, the better the financial strength rating of the EU reinsurer, the lower the collateral requirement:

Secure—1 (0% Collateral)	Secure—4 (50% Collateral)
Secure—2 (10% Collateral)	Secure—5 (75% Collateral)
Secure—3 (20% Collateral)	Vulnerable—6 (100% Collateral)

This provides a better mechanism for U.S. insurers to judge the solvency and claims paying ability of EU reinsurers before they decide whether to do business with them, which ultimately protects consumers and policyholders who want assurance that payment of their claims will not be impacted by EU reinsurers with weak

[1] To put the issues relating to reinsurance collateral in context, it should be noted that the states have long required EU reinsurers to post collateral for their U.S. obligations given differences in EU accounting systems, differences in the rigor of insurance regulation in the EU, and difficulty with enforcement of judgments by U.S. primary insurers against EU reinsurers in their home jurisdictions, all of which make it challenging for state regulators to rate the ability and/or willingness of EU reinsurers to pay their U.S. obligations.

financial strength ratings. The NAIC sliding scale model law also protects the U.S. guaranty fund system, which relies upon U.S. insurers to do business with reinsurers with strong financial strength ratings who will honor their U.S. obligations after a ceding company becomes insolvent.

PREEMPTIVE POWER IS UNNECESSARY TO ACHIEVE MUTUAL RECOGNITION. The covered agreement creates a process for state reinsurance collateral laws to be preempted if they are not revised to comply with the terms of the covered agreement. Allowing a covered agreement to preempt state laws puts the power of dictating U.S. regulatory policy in the hands of non-regulatory federal bodies and foreign governments. The U.S. should continue to pursue mutual recognition agreements with foreign bodies which recognize the robustness of our state regulatory system and put U.S. companies on a level playing field, but they should not overwrite state laws or otherwise sacrifice state insurance regulation to achieve those objectives. As such, covered agreements should have no preemptive power and should be limited to securing mutual recognition of the U.S. system under the EU's Solvency II regulatory regime.

OTHER SUBSTANTIVE FLAWS IN THE COVERED AGREEMENT. The covered agreement has three additional substantive flaws that might have been avoided if state regulators had a voice in the process and a seat at the negotiating table:

- The covered agreement fails to grant the U.S. regulatory system full equivalency under the EU's Solvency II regulatory regime. As a result, U.S. domiciled insurers will not be permitted to operate in the EU on the same regulatory terms as insurers domiciled in the EU.
- The covered agreement requires the states to enact a group capital requirement, contrary to the desires of the NAIC (the NAIC is in the process of developing a group capital calculation which they do not want to become to become a capital requirement).
- The covered agreement creates a "Joint Committee" with considerable authority to implement the covered agreement in the U.S., but its members will not include anyone representing state insurance regulatory authorities.

NO MEANINGFUL CHECK & BALANCE BY CONGRESS. The law which governs the covered agreement negotiation process is also flawed by the absence of any meaningful check and balance by Congress. Under the current process, the Administration can unilaterally preempt state insurance laws through a covered agreement. The only Congressional check on this power is a 90 day layover requirement (a covered agreement may not be implemented until 90 days after it is filed with Congress). In contrast, the EU requires two legislative approvals before implementation. Congress needs to have check and balance power over covered agreements which is as meaningful as the EU's check and balance power over them.

CONCLUSION: RENEGOTIATE THE FLAWED COVERED AGREEMENT. The current law under which covered agreements are negotiated needs to be reformed by Congress to address the deficiencies identified above. Once that occurs, the Administration should return to the negotiating table with state insurance regulators, and, with the benefit of an open and transparent process and meaningful checks and balances, seek a covered agreement which grants mutual recognition and Solvency II equivalence to U.S. insurers doing business in the EU.

For Further Information Please Contact:

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LLOYD'S

JOSEPH P. GUNSET
General Counsel

February 24, 2017

The Honorable Sean Duffy
Chairman
Subcommittee on Housing & Insurance
Committee on Financial Services
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Emanuel Cleaver
Ranking Member
Subcommittee on Housing & Insurance
Committee on Financial Services
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Duffy and Ranking Member Cleaver:

During the course of your Subcommittee's hearing on the U.S.-EU Covered Agreement on February 16th, a statement was made that may have left the impression that Lloyd's of London had failed to pay a claim due to bankruptcy. We wish to correct for the hearing record any misimpressions that may have arisen from that statement.

In fact, Lloyd's has never failed to pay a valid claim, and certainly has never gone "bankrupt" nor used financial condition to avoid any claims. Lloyd's has a long and deep history of insuring and reinsuring the American economy, writing both specialist and catastrophic risks. Lloyd's reputation in the United States was cemented in the aftermath of the 1906 San Francisco earthquake, when Lloyd's leading underwriter Cuthbert Heath on behalf of the market famously instructed their San Francisco agent to "pay all of our policyholders in full, irrespective of the terms of their policies".

Since the first Lloyd's American Trust Fund was voluntarily established by Lloyd's in 1939 on the eve of World War II to reassure U.S. clients, Lloyd's has maintained trust funds in the United States available to respond to any valid claims judgment against Lloyd's Underwriters. Today these trust funds stand at more than $12.3 billion.

More recent examples of Lloyd's steadfast commitment to the U.S. include the $7.8 billion in insured losses that the Lloyd's market paid arising out of the September 11th terrorist attacks, and $10.1 billion in insured losses Lloyd's paid arising from the 2005 hurricane season (Hurricanes Katrina, Rita, and Wilma). This is a relationship Lloyd's is proud of and continues to build upon.

So to reiterate, Lloyd's has always paid all valid claims in the United States, and has certainly never failed to honor a claim due to the financial condition of any participant in the Lloyd's market.

We are grateful for the opportunity to correct the record.

Respectfully submitted,

Joseph P. Gunset

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ODYSSEYRE

Peter H. Lovell
General Counsel

February 15 2017

The Honorable Sean Duffy
United States House of Representatives
1208 Longworth House Office Building
Washington, D.C. 20515

Dear Chairman Duffy:

I write to you on behalf of OdysseyRe Group, which consists of insurers based in the United States and United Kingdom under the Hudson and Newline banners, as well as Odyssey Reinsurance Company ("OdysseyRe"), a US-based reinsurer operating in over 100 countries around the world, including the European Union. The OdysseyRe Group has more than $10 billion of assets and over 950 employees worldwide, 671 of whom are located in the US.

I want to express our Group's full support for the "Covered Agreement" that was recently concluded by representatives of the US and the EU, which currently lays with four congressional committees in accordance with the Dodd-Frank Act. As you know, this agreement addresses (and provides relief) in three areas of great concern to US-based reinsurers doing business in the EU, which relate to (1) local presence requirements, (2) collateral requirements, and (3) the imposition of group supervision beyond local EU operations, to upstream portions of a US insurance group.

OdysseyRe has recently experienced first-hand the negative consequences of local presence and collateral requirements in the EU, and will benefit greatly from the ability to freely conduct business throughout the EU without having to first establish a branch office in every EU country, and without having collateral requirements imposed on us that are both cumbersome and costly to satisfy. We also stand to benefit from the group supervision relief provided by the Covered Agreement, which would protect the OdysseyRe Group from the imposition of supervision by EU regulators beyond our EU operations, as currently required by the EU system of regulation known as Solvency II.

In fact, in recognition of the US's entry into the Covered Agreement in mid-January, two EU countries which had introduced local presence and collateral requirements during 2016 have agreed to immediately forbear from enforcing these requirements against US reinsurers like OdysseyRe, allowing OdysseyRe to once again freely conduct reinsurance business in these two EU countries, which account for more than twenty million dollars of premium income for OdysseyRe. The Covered Agreement has therefore already brought immediate and valuable relief for OdysseyRe.

The commitment by these countries to forbear, however, is expressly contingent on the Covered Agreement remaining on course and becoming effective. OdysseyRe would immediately suffer catastrophic dislocation in respect of its business in these two countries should the Covered Agreement fail to come into effect, and suffer even greater consequences in the future throughout the rest of the EU.

We therefore respectfully urge your support of the Covered Agreement, lest we lose this immediate and tangible benefit, and the larger future benefits the Covered Agreement provides to US reinsurers like OdysseyRe.

Respectfully submitted,

Peter H. Lovell
General Counsel

RAA
REINSURANCE ASSOCIATION OF AMERICA

February 15, 2017

The Honorable Sean Duffy
Chair, Subcommittee on Housing and Insurance
House Financial Services Committee
United States House of Representatives
Washington, D.C. 20515

Re: RAA Strong Support for U.S.-EU Covered Agreement

Dear Chairman Duffy:

The Reinsurance Association of America (RAA) is the leading trade association of property and casualty reinsurers that do business in the United States. RAA membership is diverse, including reinsurance underwriters and intermediaries that are based in the U.S. and do business around the globe as well as non-U.S. companies that choose to either be licensed in the U.S. or to conduct business on a cross-border basis. For all of these companies, diversification of their business across the globe and across various lines of business is critical.

This letter is respectfully submitted in strong support of the Covered Agreement recently concluded between the U.S. and EU. First, the strength of the state-based insurance regulatory system is officially acknowledged in an international agreement for the first time. The Preamble of the Agreement explicitly provides that the Parties "respect[] each Party's system for insurance and reinsurance supervision and regulation." This formal acknowledgement is useful for many reasons, including as support for the United States' argument that the International Capital Standard being developed by the IAIS should accommodate the U.S. regulatory approach to capital. Second, the benefits of the Covered Agreement to U.S. based companies doing business in the European Union are clear and substantial. The Covered Agreement provides regulatory certainty and resolves recent market access issues for U.S. companies doing business in Europe. Per the terms of the Agreement, U.S. companies have already received access to previously closed markets. Third, the Agreement forbids the imposition of collateral against U.S. companies in Europe and prohibits the imposition of the European Union's group supervision rules beyond local EU operations to upstream entities of a U.S. Group.

If the Covered Agreement is not implemented, there is no "Plan B." The NAIC initially advised the EU that it wished to pursue equivalence only to change course to not seek equivalence when it became clear that the U.S. would have to make substantive changes to its regulatory system. And now that the U.S. has negotiated a deal that in several instances is better than equivalence and which does not have the obligations to make regulatory changes that would be required under a Solvency II equivalence determination, the NAIC and others seek to derail the Agreement. And their only suggestion is to "go back to the drawing board." Seeking to renegotiate this Agreement is potentially very damaging and counterproductive to U.S. interests.

It is notable that the U.S. is receiving these substantial benefits in exchange for something the NAIC unanimously voted do in 2011 (and received nothing from the EU in exchange for doing) – reduce collateral across all the states, in most cases to 10 or 20%. There is no need to relitigate that issue now.

Several parties attempt to characterize large passages of the Agreement as ambiguous, warranting renegotiation or some undefined official clarification. The Agreement provides for a Joint Committee "for consultation and to exchange information on the administration of the Agreement and its proper implementation." This is the appropriate process to seek clarifications for implementing the Agreement, not reopening the negotiations.

We urge Congress to see past certain parties' philosophical dislike for any federal role in negotiating an international agreement involving (re)insurance regulation as well as the possibility of limited preemption, and to focus on the real benefits achieved in the Agreement. We ask that Congress support the Administration signing the Covered Agreement thereby enabling U.S. companies to receive the substantial benefits it affords and which they would not otherwise receive.

Sincerely,

Frank Nutter

Franklin W. Nutter
President

TransRe

February 17, 2017

The Honorable Sean Duffy
United States House of Representatives
1208 Longworth House Office Building
Washington, DC 20515

Dear Chairman Duffy:

Transatlantic Reinsurance Company (TransRe) appreciated the opportunity to participate in your Roundtable discussion on the US/EU Covered Agreement. We found the opportunity to engage with you and your staff as well as others in our industry an invaluable experience. We support the current Covered Agreement and encourage you and you colleagues on the Financial Services Committee and the Subcommittee on Housing and Insurance to consider carefully the positive benefits the Covered Agreement provides for US Reinsurers, their employees and their reinsureds. We also support a continuing Federal role as respects international insurance agreements. The States, while effective in matters relating to insurer supervision, insurer market conduct and policyholder protection, are constitutionally limited as respects international matters.

While there are diverging viewpoints on the need for a Covered Agreement there are some things upon we can all agree:

The emergence of Solvency II was a decade long process and the insurance industry, the NAIC and the States had adequate notice and opportunity to engage the EU on the equivalence issue. A review of press clippings quoting NAIC Staff and State Supervisors will find them to be peppered with references to the need for US Supervisors to address issues of equivalence as far back as 2008. The Solvency Modernization initiatives undertaken by the states were a direct response to Solvency II and the IAIS Insurance Core Principles.

Coincidentally, in 2008, as a consequence of discussions between TransRe and its EU Supervisors, TransRe actively sought out staff at the NAIC to encourage them to actively engage with the EU to advocate for US insurers and reinsurers operating in Europe. This request for advocacy was set against the backdrop of the NAIC and the States working furiously to open the US market to EU companies by reducing their reinsurance collateral requirements. While the Model Act for Credit for Reinsurance wove its way through committees at the NAIC it seemed to TransRe that the States were steadfastly ignoring our pleas that the NAIC and States get something from the EU in return.

Accordingly, you can understand our bewilderment, now that the Covered Agreement has been made public, that the NAIC and the States that are now critical of the Covered Agreement for failing to achieve "Equivalence" and dismissive of the achieved outcome of "Mutual Recognition." This criticism seems hollow when one considers that: (a) despite nine years of advance notice the NAIC has accomplished little if anything of benefit to US Companies writing business in the EU while making it significantly easier for EU companies to do business in the US, and (b) Senator Ben Nelson, NAIC CEO, and then President of the NAIC, Commissioner Adam Hamm, specifically put the EU on notice that the US regulatory was "not pursuing an equivalence determination" (see attached July 2014 NAIC letter).

TransRe fully supports our effective and proven State-based supervisory system in the United States. However, our system, for all its strengths, is limited in its ability to provide the advocacy, support and authority to allow US domestic reinsurers to operate on an equal footing in the global marketplace. The current Covered Agreement largely accomplishes this with the EU and serves as notice to the emerging and developed markets elsewhere that the supervisors of the two largest global reinsurance markets have reached an agreement as to the others effectiveness and quality. The Covered Agreement process itself may be improved, and we encourage this be done within the confines of the CHOICE Act, but the current Covered Agreement provides immediate assistance to US Reinsurers and meets or exceeds the NAIC stated goals for the past nine years.

In conclusion, we see the Covered Agreement as an endorsement of the strength and effectiveness of the State-based system and a welcome demonstration of State and Federal support for US Companies that seek to operate in the EU. Further we see this as a powerful indicator to supervisors in those developed and emerging markets that look to our nation and the EU for guidance. TransRe thanks you for your leadership on this important process and looks forward to working with you on this and the other key issues facing this nation.

Warmest regards,

Edward J Kelley

Edward James Kelley, Sr.
Senior Vice President and Deputy General Counsel

Encl.

NAIC National Association *of* Insurance Commissioners & *The* CENTER *for* INSURANCE POLICY *and* RESEARCH

July 11, 2014

Mr. Jonathan Faull
Director General, Internal Market and Services
European Commission
1049 Brussels
Belgium

Dear Mr. Faull:

Thank you for your letter of June 6th regarding your views on the "Way Forward Project" and for your assessment of the US regulatory system in the context of the Solvency 2 equivalence requirement.

We agree that the Project has been useful in terms of enhancing mutual understanding of the US and EU regulatory systems. As our collective jurisdictions represent nearly two-thirds of the global insurance market, shared confidence in our different regulatory approaches is important to reinforce the transatlantic insurance market and ensure effective cross border supervision of global firms.

As you know, U.S. state insurance regulators are not pursuing an equivalence determination. While it is possible to compare our respective statutory authorities on paper, it would be challenging to conduct a comprehensive comparison of our two regulatory systems in practice until Solvency 2 is fully operational and the outcomes it produces based on actual experience are better understood.

There are clear structural and legal differences between our two supervisory systems, but we continue to believe that the US regulatory system results in outcomes for insurers and policyholders that we hope Solvency 2 will achieve once it is fully implemented. This belief is based on real experience during periods of recession and great stress, hard and soft markets, low interest rates, and increasing frequency and severity of catastrophic events. Irrespective of those views, any inflexibility in the equivalence process that precludes the Commission from reaching a similar conclusion about the efficacy of our system is entirely self-imposed. Equivalence is a function of European law subject to the Commission's interpretation, so in lieu of delineating changes to the US supervisory system that by all accounts is among the most effective in the world, the Commission should instead reevaluate whether the equivalence mandate deserves to be reconsidered given its potential negative impact on US and European firms and policyholders.

Sincerely,

Membership of the NAIC International Insurance Relations Leadership Group

Senator Ben Nelson
NAIC CEO

Adam Hamm, Chair
NAIC President
North Dakota Insurance Commissioner

EXECUTIVE OFFICE • [illegible]
CENTRAL OFFICE • [illegible]
CAPITAL MARKETS & INVESTMENT ANALYSIS OFFICE • [illegible]
www.naic.org

July 3, 2014
Page 2

Monica J. Lindeen, Vice Chair
NAIC President-Elect
Commissioner, Montana Securities and Insurance

Michael F. Consedine
NAIC Vice President
Pennsylvania Insurance Department

Sharon P. Clark
NAIC Secretary-Treasurer
Kentucky Department of Insurance

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Director, Missouri Department of Insurance

Bruce R. Ramge
Director, Nebraska Department of Insurance

Gordon I. Ito
Hawaii Insurance Commissioner

Chester McPherson
Acting Commissioner
D.C. Department of Insurance, Securities and Banking

Sandy Praeger
Kansas Insurance Commissioner

Benjamin M. Lawsky
Superintendent
New York State Department of Financial Services

James J. Donelon
Louisiana Insurance Commissioner

Julie Mix McPeak
Commissioner
Tennessee Department of Commerce and Insurance

Thomas B. Leonardi
Connecticut Insurance Commissioner

The Honorable Denny Heck
425 Cannon House Office Building
United States House of Representatives
Washington, DC 20515

Dear Congressman Heck:

On behalf of the Intergovernmental Policy Advisory Committee on Trade (IGPAC), a trade advisory committee appointed by the United States Trade Representative (USTR), which provides trade policy advice on matters that have a significant relationship to the affairs of state and local governments, I wanted to express our concern regarding the covered agreement between the European Union (EU) and the United States.

As one of the IGPAC's main concerns has always been the possibility that state laws could be preempted or found inconsistent under trade agreements, it pressed the USTR to brief the committee on the negotiations of any covered agreement since the Dodd-Frank bill was enacted. After it was reported that the United States and the EU intended to negotiate a covered agreement, on multiple occasions in 2015 and 2016, the IGPAC requested that USTR and the Treasury Department closely consult with relevant stakeholders and provide regular briefings to the IGPAC throughout the negotiations in light of the potential for this agreement to impact State sovereignty; discriminatory actions by EU member countries; and potential National Treatment violations by the EU. Unfortunately the Treasury Department and USTR failed to honor this promise and provided only one superficial briefing in December 2015 before the first round of the negotiations and failed to provide <u>any</u> briefings during the ongoing negotiations. With the conclusion of the agreement, the IGPAC has still not yet received a briefing on the potential impact this agreement may have on State sovereignty and its impact on consumer protection.

Furthermore, IGPAC Members were advised that state insurance regulators would have a meaningful role during the negotiations, however only a small group were included as observers and were unable to consult with their fellow regulators, legislators or Governor's offices. The lack of transparency to the IGPAC and other stakeholders regarding the nature and progress of the covered agreement negotiations is extremely concerning. The agreement should have been negotiated in collaboration with the States and their relevant experts at the table with frequent consultation of the IGPAC. This lack of transparency sets a dangerous precedent for future agreements. Consequently, we would urge that the agreement be renegotiated with a more transparent process that is fully inclusive of the State insurance regulators to ensure that the agreement is in the country's best interests and does not sacrifice key consumer protections.

Sincerely,

Robert C. Hamilton

Robert Hamilton
Chairman, IGPAC

SEAN UNITED STATES REPRESENTATIVE
DUFFY
PROUDLY REPRESENTING WISCONSIN'S 7TH DISTRICT

QUESTIONS FOR THE RECORD

Hearing: "Assessing the U.S.-EU Covered Agreement"
Date: February 16, 2017

Mr. Charles Chamness

1) Many of your members are purchasers of reinsurance. Are you concerned about the zeroing out of reinsurance collateral requirements from a consumer protection standpoint? From a cost standpoint, what will the impact of eliminating reinsurance collateral be on those who may choose to reach voluntary agreements with reinsurers to post collateral?

   Answer: We are concerned about the lack of collateral in place for our members, especially if collateral is not required for reinsurers with poorer credit ratings. The NAIC model provides a staggered approach to collateral in the model law that would increase the collateral requirements for reinsurers with lower credit ratings. The lack of consideration of the credit-worthiness of reinsurers under the covered agreement is a major concern.

2) A majority of members of the National Association of Mutual Insurance Companies are smaller companies that may not have plans to expand their business to international markets. Yet, the Association has voiced significant concerns about the authority of the covered agreement to allow a potential federal preemption of state regulators. Why is this issue of preemption important to NAMIC when the agreement appears to only affect larger companies operating in both the U.S. and international markets? How could Congress ensure that its oversight role is a firewall to protect state regulatory systems, as outlined in the McCarran–Ferguson Act?

   Answer: Simply put, it does not only affect larger companies doing business internationally, which is the problem. Those U.S. insurers who do not have international business – which is the *vast majority* of U.S. insurers – are the only ones who do not benefit from this agreement, and yet those same companies will lose the collateral they value from European reinsurers due to federal preemption. The covered agreement wins some minor points, if somewhat ambiguously, for the large international companies and takes reinsurance collateral away from the U.S. only companies of all sizes. Additionally and of equal importance, it also impacts the U.S.-only companies by insisting the states create a new group capital requirement which is in opposition to the legal entity regulation on which the U.S. system is based. Simply stated, U.S.- only companies get nothing from this agreement but the loss of reinsurance collateral and additional and inappropriate regulation in the form of a new group capital standard.

All Witnesses

3) In the EU, both the European Council and the European Parliament must affirmatively approve or reject the covered agreement. In the U.S., Congress doesn't even have the power to expedite the rejection of such an agreement much less approve it. As the Financial Services Committee considers this agreement, and potential future international insurance agreements, should we consider a new and more robust role for Congress?

   Answer: Absolutely, NAMIC agrees that Congress should have a more robust role. The lack of a role is especially troubling when this type of trade activity impacts state or federal laws without a legislative role. NAMIC has long called for Congress to be more involved in this process and at a minimum should have an up-or-down vote on any covered agreement reached by the executive branch.

4) With this covered agreement, FIO has the power to preempt a State insurance measure if the Director determines that the measure "results in less favorable treatment of a non-United States insurer domiciled in a foreign jurisdiction that is subject to a covered agreement than a United States insurer domiciled, licensed, or otherwise admitted in that State." Although not explicitly cited in the statute, this is generally understood to be a reference to a reinsurance collateral agreement with the EU. If the agreement enters into force, do we still need covered agreement authority as outlined in Dodd-Frank?

   Answer: NAMIC does not think that the authority was needed in the first place, and most certainly is not needed going forward.

5) Some have expressed concerns that the Executive Branch could use the authority under Dodd-Frank for a covered agreement to achieve an agreement on capital standards with the International Association of Insurance Supervisors (IAIS). Do you think that the language in Dodd-Frank for covered agreements gives the Executive Branch that authority?

   Answer: The current covered agreement demonstrates exactly how an administration can allow a foreign jurisdiction like the EU to try and backdoor new foreign standards into the U.S. The EU simply invented regulatory pressure on U.S.-based companies under the guise of Solvency II's equivalency determination, and is now using the covered agreement to insist on changes to U.S. law and practice in order to make that pressure disappear. This is what the group supervision provision of the covered agreement is about.

We are also concerned about future activist FIO directors broadly interpreting the language in Dodd-Frank to give the FIO and USTR the authority to address other issues. These could take the form of new or different capital standards (whether or not in an agreement through the IAIS) or governance standards, which could all be considered to be under the statutory language of "prudential measures." This would be an abuse of the covered agreement authority. We do not believe covered agreements should deal with issues that can and are being resolved by the state insurance commissioners or through their organization the NAIC.

Questions for the Record
Rep. Blaine Luetkemeyer (MO-03)
"Assessing the U.S.-EU Covered Agreement"
Committee on Financial Services
Subcommittee on Housing and Insurance
February 16, 2017

To Charles Chamness, NAMIC

1. You have advocated that this Covered Agreement be renegotiated. That will no doubt take time. What can be done to immediately assist U.S. based companies on the market access issues and the expensive Solvency II compliance costs that would otherwise be addressed by this Covered Agreement?

Response:

We do not believe that the market access issues and Solvency II compliance costs are ultimately addressed by this covered agreement as it does not adequately resolve the question of U.S. equivalence or mutual recognition. Therefore another solution is needed. Simply signing a flawed agreement and hoping for the best down the line should not be the U.S. strategy. Solvency II was implemented on January 1, 2016 and yet the EU stayed the enforcement for U.S. companies for over a year as the covered agreement was being negotiated. They can simply do that again. Or they could grant the U.S. equivalence and remove the problems they invented in the first place. Regardless, we do not believe reopening negotiations will make the EU walk away from the table when they stand to gain $40 billion in reinsurance collateral relief.

U.S. House of Representatives Financial Services Committee
Hearing: "Assessing the U.S. – EU Covered Agreement"
February 16, 2017
Michael T. McRaith
Replies to Questions for the Record

Chairman Duffy

Question Number One

The Covered Agreement (Agreement) opened the entire EU reinsurance market to U.S. reinsurers, spared U.S. industry operating in the EU potentially billions of dollars in compliance costs, and embraced the U.S. state regulatory approach to insurance group supervision.

The Agreement applies only to, and provides clarity for, U.S. and EU insurers that operate in both jurisdictions. Notably, the benefits are not mutually exclusive in that a positive outcome for EU industry stakeholders can also benefit U.S. interests.

EU insurers and reinsurers insure millions of American families and businesses and employ tens of thousands of Americans in states around our country. EU-based holding companies own high profile U.S. property and life insurers. EU-headquartered insurers and reinsurers pay billions to assist the United States in post-disaster recovery. For example:

- EU insurers and reinsurers paid more than $12.2 billion in claims following the terrorist attacks of September 11, 2001, an event for which 64% of all claims were paid by reinsurers. Lloyd's paid more than 11% of all 9/11 claims.

- Following the devastation of Hurricanes Katrina, Rita and Wilma, more than 22% of all claims were paid by EU insurers and reinsurers, with Lloyd's paying nearly 10% of the total.

- Of the total insured claims of $18.715 billion from Superstorm Sandy, $5.3 billion was paid by EU-headquartered insurers and reinsurers, and approximately $2.5 billion was paid by Lloyd's.

This reply identifies only the legal benefits conferred upon the United States and its stakeholders (consumers and industry), and does not describe the financial and commercial benefits for those stakeholders.

The Agreement is drafted in language, and provides benefits, that apply equally to the United States and the EU. The following list of legal benefits conferred on the United States by the Agreement cites directly to the relevant Article and Paragraph:

a. Preamble: the Preamble reflects the understandings and acknowledgements of the United States and the EU with respect to the Agreement. While each is an important statement, three warrant specific mention:

"Sharing the goal of protecting insurance and reinsurance policyholders and other consumers, while respecting each Party's system for insurance and reinsurance supervision and regulation";

"Taking into account information exchanged on each Party's regulatory frameworks and after careful consideration of these frameworks";

"Acknowledging the need for a group capital requirement or assessment for insurers and reinsurers forming part of a group that operates in the territory of both Parties, and that a group capital requirement or assessment at the level of the worldwide parent undertaking can be based on the approach of the Home Party[.]"

b. Article 1 – Objectives

While Article 1 does not, in itself, confer any legal benefits for U.S. stakeholders, the Objectives articulate the goals of the Agreement. While each is important and are addressed in the following substantive Articles, these goals describe the outcome of the Agreement:

(a) Elimination of local presence requirements for U.S. and EU reinsurers operating in the other jurisdiction.

(b) Elimination of collateral requirements for U.S. and EU reinsurers operating in the other jurisdiction.

(c) Prohibit the application of group supervision by an EU regulatory authority except to the extent that the U.S. insurer has operations or activities occurring in or originating from the EU, including with respect to solvency and capital, governance and reporting.

c. Article 2 — Definitions

d. Article 3 — Reinsurance

Article 3 describes the Parties' affirmative commitments with respect to reinsurance.

Paragraph:

1. and 2. U.S. reinsurers will not be subject to collateral requirements, or any requirement of similar impact, when operating in the EU unless EU reinsurers are also subject to those requirements in the EU. This prohibition applies both to contractual arrangements and to regulatory credit to a ceding insurer for the purchased reinsurance.

3. U.S. reinsurers will not be subject to local presence requirements (i.e. the establishment of a subsidiary, holding company, or other legal entity) or any requirement of similar impact, when operating in the EU.

4(a) - (l). Relief from local presence and collateral obligations for an EU reinsurer in the United States is dependent upon the EU reinsurer meeting financial condition and market conduct standards. The details of these standards, which remove excessive regulation, track existing state-based law and regulation.

5. In addition to the information required by paragraphs 4(a) - (l), reinsurers may voluntarily provide information to regulatory authorities.

6. In the event that an EU reinsurer fails to meet the standards and requirements of paragraph 4, then U.S. insurance authorities may re-impose collateral requirements on that EU reinsurer.

7. Subject to applicable law, U.S. ceding insurers can negotiate any provision in any reinsurance agreement, including for collateral.

8. Existing U.S. reinsurance agreements are not affected by the Agreement, i.e. the Agreement does not have a retroactive effect. Consistent with basic contract law, reinsurance agreements cannot be unilaterally amended. An amendment to a reinsurance agreement can be limited to the targeted subject matter of the amendment without changing the remaining provisions of the agreement.

If, for example, a reinsurer changed its name, then the parties to that reinsurance agreement could agree to amend the existing reinsurance agreement with respect to the name change only, which would not alter the agreement's requirement for collateral.

These provisions are drawn from NAIC Model Regulation 786 (Credit for Reinsurance).

9. If the Agreement were terminated, then the United States and the

EU can again require the posting of collateral or the establishment of a local presence for a reinsurer domiciled in the other jurisdiction.

e. Article 4 — Group Supervision

This Article describes the mutual affirmation of group supervision practices of the United States and the EU, and describes group supervision practices to be adopted by both the United States and the EU upon the date of provisional application, (i.e. date of signature, as provided in Article 10, Para. 2(a)).

Article 4 applies only to those U.S. insurers operating in both the United States and the EU.

Article 4 acknowledges that the United States and the EU have different approaches and systems with respect to insurance group supervision, and provides clarity regarding the interaction of those approaches and systems going forward.

Paragraph:

(a) Recognizing the value of supervisory colleges, the Agreement clarifies that only U.S. insurance supervisors will supervise U.S. insurers at the worldwide group level. In other words, EU supervisors can apply EU law and regulation to U.S. insurers only for operations and activities that occur in or originate from the EU. This limitation applies to all aspects of group supervision, including solvency and capital, governance, and reporting.

In other words, U.S. insurers are supervised at the worldwide group level as determined by U.S. state insurance regulators.

(b) Subject to Article 3, U.S. insurers and reinsurers operating in the EU are subject to EU law and regulation only for purposes of operations and activities occurring in or originating from the EU.

(c) U.S. insurers are required to prepare only a U.S. state-based Own Risk Solvency Assessment (ORSA) at the worldwide group level, not both a U.S. and an EU ORSA. The summary report of the U.S. ORSA can be shared with EU supervisors through the insurer's supervisory college. In other words, at the worldwide group level, U.S. insurers will complete an ORSA consistent with U.S. state regulatory practices.

(d) The required elements of the ORSA, as described in this paragraph, are drawn from the NAIC Risk Management and Own Risk and

Solvency Model Act (#505) and the NAIC ORSA Guidance Manual.

(e) If the ORSA of an EU insurer or reinsurers reveals a serious threat to U.S. policyholders, then the U.S. insurance regulator may consult with the insurer's lead EU supervisor and may impose preventive, corrective or responsive measures.

(f) U.S. insurers operating in the EU report at the worldwide group level only to the lead U.S. insurance supervisor unless the information to be reported reveals a direct threat to activities or operations occurring in or originating from the EU. In other words, at the worldwide group level, U.S. insurers report consistent with U.S. state regulatory practices.

(g) U.S. regulators retain the ability to ask for information about non-U.S. activities that may pose a serious threat to the ability of an EU insurer or reinsurer to pay its claims in the United States.

This language tracks the "windows" of the NAIC Model Holding Company Act (#440) provisions that allow state insurance regulators to "scrutinize group activity and assess its potential impact on the ability of the insurer to pay its claims."

(h) As with all of Article 4, the group capital calculation applies only to U.S. insurers that operate in the EU. U.S. insurers and reinsurers operating in the EU are relieved of the EU's Solvency II group capital requirement upon the date of provisional application, i.e. the date of signature (Article 10, Para. 2(b)).

U.S. state insurance regulators who, in reply to international developments, have been developing a group capital calculation since 2014, have five years from the date of signature (Article 10, Para. 2(a) and 2(e)) to develop the group capital calculation for the subset of U.S. insurers operating in the EU. For that five (+) year period, and upon completion, U.S. insurers operating in the EU are not thereafter subject to reporting or maintaining the Solvency II worldwide group capital requirement. The language is not prescriptive in terms of the mechanics or specifics of the group capital calculation, but defers to the ongoing work of U.S. state insurance regulators.

The language regarding "authority to impose preventive, corrective, or otherwise responsive measures on the basis of the assessment, including requiring, where appropriate, capital measures" is intentionally broad. This language accommodates both the U.S. state regulatory approach (i.e. at the entity level) and the EU Solvency II approach (i.e. at the holding company level).

(i) If the EU exercises enhanced group supervision over a U.S. insurer for purposes of financial stability, then the United States can terminate the Agreement.

f. Articles 5 and 6 — Exchange of Information and Annex

These Articles encourage continued and enhanced exchange of confidential information across borders and encourage U.S. and EU supervisors to utilize the template attached as an Annex to the Agreement.

g. Article 7 — Joint Committee

Article 7 provides for the establishment of a Joint Committee to address questions of the Agreement's interpretation and implementation.

h. Article 8 — Entry into force

The Agreement enters into force seven days after the Parties exchange written notice that internal approval processes have been completed. However, timing for the effective date of the Agreement provisions is specified in Article 10.

i. Article 9 — Implementation of the Agreement

Article 9 describes that the EU and the United States shall take all measures to implement and provisionally apply the Agreement.

j. Article 10 — Application of the Agreement

The Agreement is entirely cross-conditional. Neither the EU nor the United States receive the benefits of the Agreement without providing the benefits of the Agreement. For example, if, five years from the date of signature, the EU were to reject the U.S. state regulatory approach to worldwide group capital for U.S. insurers operating in the EU, then the EU would relinquish the benefits of the Agreement for EU consumers and industry.

1. The Agreement applies to U.S. insurers operating in the EU on the date of entry into force, or the date of signature, whichever is later.

2. (a) U.S. insurers and reinsurers operating in the EU are relieved of Solvency II worldwide group requirements upon signature of theAgreement (i.e. the date of provisional application).

(b) Provided that the U.S. state insurance regulators comply with Articles 3 and 4, then the provisions and benefits of Article 3 and 4 will be received by U.S. consumers, insurers, and reinsurers.

(c) The exercise by the EU of enhanced supervision over a U.S. insurer or reinsurer for EU financial stability purposes (and vice versa) can be grounds for termination of the Agreement.

(d) U.S. state insurance regulators adopted the NAIC's reinsurance collateral reform as a national accreditation standard effective January 1, 2019 (i.e. every state would have a conforming law or regulation by that date). The Agreement provides the states with additional time, potentially into 2023, to adopt measures consistent with the Agreement.

(e) The EU will not impose a Solvency II worldwide group capital requirement on U.S. insurers and reinsurers operating in the EU for five years from the date of signature, and then only if the United States has not developed a group capital calculation as described in Article 4(h).

(f) If the EU does not meet the obligations of Article 3 with respect to the elimination of local presence requirements, then U.S. state insurance regulators may impose a worldwide group capital requirement or assessment on EU insurers and reinsurers. The inverse is also true.

(g) The EU will eliminate local presence laws within two years from the date of signature.

(h) U.S. reinsurers operating in the EU will not be subject to collateral requirements, or the equivalent, within five years from the date of signature.

(i) The Agreement provisions regarding the Joint Committee, Termination and Mandatory Consultation, and Amendment will be effective upon the date of signature.

n. Article 11 — Termination and Mandatory Consultation

Subject to the procedures established in the Agreement, the Agreement can be terminated at any time by either party.

o. Article 12 — Amendment

Article 12 sets forth the process for amending the Agreement.

Question Number Two

The Agreement opened the entire EU reinsurance market to U.S. reinsurers, spared U.S. industry operating in the EU potentially billions of dollars in compliance costs, and embraced the U.S. state regulatory approach to insurance group supervision, thereby conferring on U.S. consumers and industry the wide range of legal benefits described in reply to Question Number One.

Stakeholders were consulted extensively before and throughout the negotiation of the Agreement. For purposes of the Agreement negotiations, Treasury and USTR created and successfully utilized an unprecedented mechanism to include U.S. state insurance regulators the negotiation of an international agreement. For example, a total of ten regulators from nine states participated as members of the U.S. state insurance regulator task force that contributed significantly throughout negotiations of the Agreement, three of whom also served on FACI.

The Federal Advisory Committee on Insurance (FACI) was first created in 2011. FACI's existence and endeavors are guided by the Federal Advisory Committee Act (Pub.L. 92-463, 86 Stat. 77 (1972)). Given that Treasury and USTR engaged extensively with Congress, state regulators, and other stakeholders throughout the Agreement negotiations, and given that the Agreement provides material legal, financial and commercial benefit to U.S. consumers and industry, alteration of the FACI role would be both duplicative and unnecessary.

Question Number Seven

Congressional authority is not constrained by Title V of the Dodd-Frank Act. Further, the EU is a union of independent sovereign nations whereas every other counter-party would likely be a single nation. However, the Agreement involves prudential insurance and reinsurance measures, and is not a trade agreement. Without comment on matters of international trade, matters of prudential oversight such as those contained in the Agreement are qualitatively different. For example, Congress does not "expedite rejection" or approval of NAIC model laws and regulations.

As provided in Title V of the Dodd-Frank Act, frequent engagement with all four Congressional committees of jurisdiction was extremely meaningful and helpful throughout the negotiation of the Agreement.

Question Number Eight

Insurance markets are increasingly global, and multi-national U.S. insurers have tremendous opportunities for organic growth in the developing markets of Central and South America, Asia and Africa, and Eastern Europe. The Covered Agreement authority in Title V (the "FIO Act") of the Dodd-Frank Act may be necessary to address and resolve differences in the regulation of the business of insurance between the United States and other jurisdictions.

For example, when the FIO Act became law in 2010, few in the United States *or* the EU knew whether and, if so, when or in what form, the EU's Solvency II regime would be implemented. The Agreement illustrates that the Covered Agreement authority can resolve important issues of cross-border insurance regulation and, at the same time, provide potentially billions of dollars in value to the U.S. consumers and industry. Due to the variability of potential fact patterns in increasingly globalized insurance markets, the FIO's Covered Agreement authority has an appreciably growing value to American interests, and potential expansion of the authority may be necessary.

Question Number Nine

No. A Covered Agreement can be negotiated with one or more foreign jurisdictions.

The International Association of Insurance Supervisors (IAIS) is not a foreign jurisdiction but is a voluntary association of members formed under the laws of the Switzerland. In this sense, the IAIS is akin to the NAIC which, of course, is also a voluntary association of members formed under the laws of the United States but is not a "jurisdiction."

Further, as detailed in reply to Question Number One, the Agreement demonstrates that Covered Agreement will be used to preserve and enhance the U.S. system of insurance regulation.

Congressman Hultgren

A. Yes. Reinsurance agreements are subject to the principles of basic contract law. Amendments to contracts, regardless of the magnitude of the amendment, require an agreement of the parties to the contract. An amendment to a reinsurance agreement that could result in the reduction of collateral would require that both parties to that reinsurance agreement agree upon the amendment. Collateral could not be reduced if the ceding insurer did not also agree.

B. The Agreement does not have retroactive application. The hypothetical of a reinsurer's scheme of arrangement (a "Part VII transfer of business"), or the application of a jurisdiction's unique legal or regulatory system, depends upon numerous complex variables and cannot be answered in the abstract. However, Article 3 of the Agreement preserves the authority of a ceding insurer's U.S. state insurance regulator to re-impose collateral and other requirements on a reinsurer that fails to satisfy the Agreement's financial condition and market conduct standards. Further, a Part VII transfer would likely trigger the standard provisions of a reinsurance agreement that allow the ceding insurer to accelerate the posting of collateral

SEAN UNITED STATES REPRESENTATIVE
DUFFY
PROUDLY REPRESENTING WISCONSIN'S 7TH DISTRICT

QUESTIONS FOR THE RECORD

Hearing: "Assessing the U.S.-EU Covered Agreement"
Date: February 16, 2017

Commissioner Ted Nickel

1) Some stakeholders of the covered agreement argue that the NAIC was never going to be satisfied with a covered agreement because the very notion of a covered agreement undermines the authority of state insurance commissioners and the state-based regulatory model. Is there a better deal that you and the NAIC could live with?

I believe it would be very difficult for even proponents of the covered agreement to say that we could not have gotten a better deal or one that is at least clear on its terms. Certainly, the NAIC is open to finding more workable solutions that fit with our national state-based regulatory system. In fact, after the hearing, we sent a letter to Secretary Mnuchin to obtain a better understanding of certain aspects of the agreement in order to determine whether it is in the best interest of the United States and, if so, how to implement it. We want relief for our U.S. domiciled insurers operating in the European Union, but we also seek a deal that provides for finality and does not undermine important policyholder protections.

For one, at bare minimum, we would clarify a number of the provisions of the agreement particularly those relating to group supervision and capital. Second, the agreement should clearly resolve the equivalence question and provide recognition for the U.S. insurance regulatory system. Third, while we acknowledge that the key priority for the EU is to address collateral, if there is a renegotiation, the wholesale elimination of collateral has to be revisited. U.S. insurers and policyholders should not have to bear the full brunt of the counterparty risk posed by reinsurers. We would suggest more closely aligning the reinsurance collateral provisions to the NAIC's model law that already has been adopted by 35 states representing 2/3 of the direct written premium in this country. Under the model act, collateral is reduced on a reinsurer-specific basis only after an evaluation of the financial strength and quality of supervision of that particular reinsurer. Fourth, if the agreement is clear on its face, a joint committee should not be necessary. But if the parties believe it still will be useful, the nature of the committee, its responsibilities and its membership should be clearly spelled out in the agreement and state insurance regulators should be included among its members. Otherwise, it appears state insurance regulators will be haggling constantly from afar about the implementation of the agreement and potential preemption pursuant to the agreement. Fifth, any renegotiation process should be far more transparent and allow for the actual direct and meaningful participation of all state insurance regulators. If all insurance regulators cannot be included directly, then structures should be created to ensure all can be briefed on progress and consulted on its terms. The process should allow for more robust stakeholder consultation and congressional oversight. Finally, under the Dodd-Frank Act, state laws are potentially subject to preemption pursuant to the terms of the agreement. Preemption of law is not a step to be undertaken lightly. If we are to avoid such steps unnecessarily or acquiesce to such steps, the agreement should be clear about what we are obtaining in return.

The NAIC believes a better deal could have been made without undermining key policyholder protections. If we work together and allow full participation of state insurance regulators, we could still achieve the finality that is lacking in the current agreement, avoid undermining important consumer protections, and provide relief to U.S. firms operating in the European Union.

2) Your testimony mentions that the repercussions of this agreement will be paid for by U.S. insurers and policyholders. Can you elaborate?

Certainly there are a few large U.S. companies who operate abroad that require relief from the threat of Solvency II requirements on their operations. Although these requirements are entirely of the EU's making, we very much sympathize with those concerns. However, benefits to those international companies pale in comparison with the costs imposed by the agreement when risk is shifted from foreign reinsurers to U.S. ceding companies.

The NAIC believes that the covered agreement will completely redefine the way we regulate reinsurers and will force the NAIC to develop means other than collateral to provide U.S. policyholders the protections they need. Collateral is a proven tool to protect U.S. insurers and by extension policyholders from the counterparty risks posed by reinsurers. A similar approach is used in a myriad of other financial transactions including derivatives transactions, securities trades, etc. Insolvencies, while initially paid for by insurers, are ultimately born by states' general funds through lower than expected premium taxes from insurers because of premium tax offsets. If collateral is eliminated, ceding insurance companies and by extension policyholders will be exposed to increased risks. Insurance regulators will be forced to explore other means to protect insurers and policyholders from these counterparty risks. For example, we may have to utilize a more European approach where ceding insurance companies bear the burden of accounting for such counterparty risks through higher capital requirements. Alternatively, regulators could choose to apply collateral to all reinsurance transactions irrespective of where the reinsurer is located. In either event, the costs of the covered agreement will be borne by U.S. insurers and ultimately their policyholders, who may face higher premiums.

Questions for the Record
Rep. Blaine Luetkemeyer (MO-03)
"Assessing the U.S.-EU Covered Agreement"
Committee on Financial Services
Subcommittee on Housing and Insurance
February 16, 2017

To Commissioner Nickel

1. You have advocated that this Covered Agreement be renegotiated. That will no doubt take time. What is the NAIC's plan to immediately assist U.S. based companies on the market access issues and the Solvency II compliance costs that would otherwise be addressed by this Covered Agreement?

Commissioner Nickel on behalf of the NAIC:

At the outset, I disagree with the premise that the covered agreement significantly reduces compliance costs for U.S. firms operating in the European Union. Most U.S. firms operating in the European Union were already organized through intermediate holding companies with either capitalized insurance subsidiaries or branch operations in a manner that complied with Solvency II, particularly the EU's local presence requirements. To the extent that such firms have compliance costs associated with operating in the EU (such as reporting obligations), the terms of the agreement do little to ameliorate that. In fact, it codifies them by providing for continued EU supervision over a U.S. insurer's EU operations. Similarly, to the extent some believe the agreement prevents the EU from applying its capital and governance standards extraterritorially, the EU cannot do that today in the absence of the agreement, nor has any EU member country attempted to do so.

Further, while the agreement may provide some regulatory relief for a few U.S.-based companies operating in the EU, the erosion of consumer protections and the burdens that smaller insurance companies in the United States may have cannot be overstated. Without collateral, risk to U.S. policyholders will increase, and the NAIC will have to find ways to address reinsurance counterparty credit risk, be it higher capital requirements on U.S. ceding companies, or some other mechanism that shifts the risk to all reinsurers operating in the U.S. Of course, if a reinsurer fails to support a ceding company in the event of a catastrophe, the costs to American consumers could potentially be far greater than any perceived benefits from the covered agreement. The cost of any insolvency resulting from uncollectible reinsurance, or otherwise, will be absorbed by U.S. insurers and ultimately U.S. policyholders and taxpayers.

Nevertheless, the NAIC takes seriously the EU's disparate treatment of U.S. insurers, which is why after the hearing, the NAIC sent a letter to Secretary Mnuchin asking him to reengage the EU and seek clarification on several of the agreement's provisions. Such clarification will enable insurance regulators, the Treasury Department, Congress, and stakeholders to fully evaluate the benefits of the agreement to the U.S. And, if it the agreement is in the best interest of the U.S., such clarifications will eliminate ambiguities so that the states are not expending time and resources attempting to implement the agreement in a manner that may not meet the *expectations of the EU. In the event the agreement is not in the best interest of the U.S. insurance sector, we would hope the Treasury Department will seek renegotiation of key provisions. In any renegotiated covered agreement, we would expect the local presence requirements to be eliminated, mutual recognition and equivalence to be clearly addressed, and the resolution of ambiguities in a way that is beneficial to the U.S. insurance sector. Under the Dodd-Frank Act, state laws are potentially subject to preemption pursuant to the terms of the agreement. Preemption of law is not a step to be undertaken lightly. If we are to avoid such steps unnecessarily or acquiesce to such steps, the agreement should be clear about what the U.S. is obtaining in return.*

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April 10, 2017

The Honorable Sean Duffy, Chairman
Subcommittee on Housing and Insurance
House Financial Services Committee
U.S. House of Representatives
Washington, DC 20515

VIA Electronic Mail

RE: Answers of AIA CEO Leigh Ann Pusey to Requested Questions for the Record for Subcommittee Hearing Titled "Assessing the U.S.-E.U. Covered Agreement"

Dear Chairman Duffy:

Thank you again for the opportunity to testify before the Financial Services Committee's Housing and Insurance Subcommittee at the hearing titled "Assessing the U.S.-E.U. Covered Agreement." As requested, please find below responses to questions numbered 7, 8, & 9 that were identified in the Questions for the Record document received from your office by email on March 21, 2017 as those to be answered by all witnesses.

7) In the EU, both the European Council and the European Parliament must affirmatively approve or reject the covered agreement. In the U.S., Congress doesn't even have the power to expedite the rejection of such an agreement much less approve it. As the Financial Services Committee considers this agreement, and potential future international insurance agreements, should we consider a new and more robust role for Congress?

AIA would urge caution here. Unlike traditional international trade agreements, international insurance agreements (or "covered agreements," as they are termed under Dodd-Frank) must balance the exclusive federal foreign affairs power with the McCarran-Ferguson Act, which delegates the primary role for regulating the business of insurance to the states. If Congress assumed a more robust role, such a role would undermine the primacy of state insurance regulation, which is otherwise protected and preserved throughout Title V of the Dodd-Frank Act (in addition to being explicitly recognized in Titles I, II and X).

We believe that the Financial Services Committee can strike the right balance by amending Title V to provide a dedicated consultation mechanism for the state insurance regulators. That mechanism would be different from the Federal Advisory Committee on Insurance, and would be an exclusive policy channel for the state insurance regulators with those federal offices that are charged with executing international insurance regulatory negotiations.

8) With this covered agreement, FIO has the power to preempt a State insurance measure if the Director determines that the measure "results in less favorable treatment of a non-United States insurer domiciled in a foreign jurisdiction that is subject to a covered agreement than a United States insurer domiciled, licensed, or otherwise admitted in that State." Although not explicitly cited in the statute, this is generally understood to be a reference to a reinsurance collateral agreement with the EU. If the agreement enters into force, do we still need covered agreement authority as outlined in Dodd-Frank?

Yes. As noted in the question, the power of federal preemption envisioned by Title V of the Dodd-Frank Act is exceedingly narrow, but the value of the covered agreement authority is not. Interpreted correctly, the recently-concluded covered agreement provides valuable precedent for foreign jurisdiction acknowledgement, acceptance, and even recognition of the U.S. state-based insurance regulatory system. AIA believes that this precedent, repeated in future covered agreements with other foreign jurisdictions, provides "Team USA" with negotiating leverage in all international discussions that involve insurance prudential, supervisory, or regulatory initiatives to demand flexibility to accommodate the U.S. system and to maintain the competitiveness of the U.S. insurance industry.

9) Some have expressed concerns that the Executive Branch could use the authority under Dodd-Frank for a covered agreement to achieve an agreement on capital standards with the International Association of Insurance Supervisors (IAIS). Do you think that the language in Dodd-Frank for covered agreements gives the Executive Branch that authority?

No. There is nothing in the Dodd-Frank Act that permits the Executive Branch to bypass the state insurance regulatory system and agree to an overarching capital requirement that the states would be forced to implement. Indeed, neither the U.S. Constitution nor the Dodd-Frank Act grants the Executive Branch the power to import foreign insurance capital standards and force their adoption on the states, or enlarge state sovereign authority over the business of insurance beyond state borders. 31 U.S.C. § 313(k), added by Dodd-Frank, reinforces this point: "Nothing in this section or section 314 [covered agreements] shall be construed to establish or provide the [Federal Insurance] Office or the Department of the Treasury with general supervisory or regulatory authority over the business of insurance." As a result, the Dodd-Frank Act – even as it establishes a covered agreement vehicle – reaffirms the delegation of regulatory authority over the business of insurance to the states under the McCarran-Ferguson Act.

Respectfully submitted,

Leigh Ann Pusey

Leigh Ann Pusey
President & CEO
American Insurance Association

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