

# CURRENT ISSUES IN INSURANCE

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HEARING  
BEFORE THE  
COMMITTEE ON  
BANKING, HOUSING, AND URBAN AFFAIRS  
UNITED STATES SENATE  
ONE HUNDRED SEVENTEENTH CONGRESS  
SECOND SESSION  
ON  
EXAMINING THE INSURANCE INDUSTRY TO ENSURE IT IS PROTECTING  
AMERICANS  
SEPTEMBER 8, 2022

Printed for the use of the Committee on Banking, Housing, and Urban Affairs



Available at: <https://www.govinfo.gov/>

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U.S. GOVERNMENT PUBLISHING OFFICE

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THURSDAY, SEPTEMBER 8, 2022

U.S. SENATE,  
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,  
*Washington, DC.*

The Committee met at 9:59 a.m., via Webex and in room 538, Dirksen Senate Office Building, Hon. Sherrod Brown, Chairman of the Committee, presiding.

### OPENING STATEMENT OF CHAIRMAN SHERROD BROWN

Chairman BROWN. The Senate Committee on Banking, Housing, and Urban Affairs will come to order.

I thank my colleagues for joining us. Most of them will be here checking in or doing some—it is a remote—I mean, it is a hybrid hearing. Again, the witnesses are here in person. Thank you, the two of you, for that.

A special callout to Sneha Pandya in our office, who has been a fellow for the last year, and this is her last hearing. She is ending with a flourish, so thank you for your service to our—to the Senate and especially to our country.

Every American needs insurance, whether it is auto insurance to protect us when we are on the road or homeowners' insurance to protect the biggest investment for most families, for life insurance to cement your family's financial security in the event of a tragedy.

It is our job to make sure that the industry is protecting Americans' hard-earned money, not putting it at risk. American insurance companies are regulated by State insurance commissioners; we know that. The State-based system of insurance regulation is historic and ensures that local markets and needs are taken into consideration. The National Association of Insurance Commissioners (NAIC) coordinates State commissioners across all jurisdictions to identify and address risks to the entire system.

In the Wall Street Reform Act Congress created a few years ago, a decade or so ago, Congress created the Federal Insurance Office within the Treasury Department to promote national coordination in the insurance sector. It is common sense; insurers operate across all State jurisdictions and internationally.

I am pleased to have both the Maryland Commissioner, Kathleen Birrane, on behalf of the NAIC, and Director Seitz of FIO testify today. Thanks for your public service on all levels.

If we are going to keep Americans' hard-earned money safe, it is more important than ever that they work together.

We will explore many topics today. For example, 3 months ago, Lockheed Martin transferred \$4.3 billion of its pensions to Athene

Holding, an insurance holding company specializing in life insurance and owned by the private equity firm, Apollo Global Management. Overnight, Lockheed Martin employees and retirees were notified that their pensions would be managed by Athene and no longer governed by ERISA or the Pension Benefit Guaranty Corporation. Many employees are very, exceptionally, nervous about that. It is one recent example of private equity giants' expansion into people's pensions and into the insurance industry.

We know that workers end up worse off when Wall Street private equity firms get involved. We have seen it over and over, in industry after industry.

In March, I asked NAIC and FIO to look into private equity's expansion into similar pension-risk transfer transactions. We need to understand the risks to workers whose financial security depends on pension and retirement programs. NAIC and FIO provided thoughtful responses to my letters. Thank you for that.

NAIC has been monitoring the risk-taking behavior of private equity-owners insurers. FIO has done similar work and also looked at the wider interconnectedness of insurance and reinsurance markets across the world. Those connections have added to systemic risk concerns because U.S. insurance companies depend even more on the financial health of insurance companies outside the United States. Taken together, our insurance authorities are focused on these emerging and complex risks to safeguard our economy.

Our communities and our families rely on insurance companies to protect their loved ones, their homes, their small businesses, and so many parts of their lives. We cannot ignore when risks buildup or firms behave irresponsibly. We know who always pays the price when they do. It is rarely insurance executives. It is not Wall Street. It is not private equity executives. It is workers and families. It is taxpayers who are forced to bail out AIG a decade and a half ago. That should never happen again.

It means looking around the corner to make sure industry and agencies are prepared for risks as they develop. As more Americans face increasingly severe climate catastrophes, wildfires, hurricanes, every year, we need to help communities prepare, and we need to ensure that insurance watchdogs and the companies they oversee are also prepared. In the aftermath of some of these natural disasters, we have seen instances where insurers either raise prices or actually stop offering insurance altogether, leaving families, leaving businesses struggling to find affordable coverage as they work to rebuild their lives and rebuild their communities.

We know this industry has a long history of racial discrimination, just like so many other big industries. Black and Brown families face more difficulty across the board in getting insurance. We have seen this happen in auto insurance. Particularly earlier this year, the *New York Times* reported that customers, insurance agents, and employees sued State Farm for discrimination in the workplace and in paying out claims.

My colleague, Chairwoman Waters in the House, has been working on learning more about this as well. Her committee recently requested information about large life and P&C insurers' involvement in financing chattel slavery.

I am glad FIO and NAIC are also working on this and

NAIC is investigating through its Special Committee on Race and Insurance. I look forward to reviewing FIO's upcoming report on availability and affordability of auto insurance. I hope it will shed more light on racial equity in assessing this insurance—in accessing this insurance.

Finally, later this year, the International Association of Insurance Supervisors will need to consider whether the U.S. insurance system's review of capital adequacy standards meets international criteria. Because we regulate insurance differently in the United States, where State and local markets and international markets are served by the same companies, it is important that representatives of the U.S. system, like you, like FIO, like NAIC, advocate for fair treatment by international regulators. And now that the Fed Vice Chair for Supervision has been confirmed, Michael Barr and the offices testifying here today will get to work with international counterparts in this process.

All of these issues show how critical the work that you two do is to our economy's health and stability. I expect FIO and NAIC to prioritize monitoring these risks in their ongoing work.

Senator Toomey.

#### **OPENING STATEMENT OF SENATOR PATRICK J. TOOMEY**

Senator TOOMEY. Thank you, Mr. Chairman. Welcome to our witnesses. It has been a while since our Committee has held a hearing on the insurance industry, and so I welcome the occasion this morning.

There are a few topics in particular I would like to touch on today. One is the importance of the State-based insurance regulation model that we have, efforts to develop international insurance standards, efforts to use the insurance industry to effect changes in social policy, proposals to create a federally guaranteed pandemic risk insurance program, and finally, the importance of risk-based pricing.

So I think it is important to start by reminding everyone, as the Chairman alluded to, that insurance firms are primarily regulated at the State level. Insurers have been chartered and regulated by the States for the past 150 years. When it comes to insurance, the Federal Government has a really very extremely limited regulatory role, and I see little need to expand that. The system works well for consumers and for the industry, and that is one reason we need to pay close attention to efforts to develop and implement international insurance standards by international bodies.

In particular, I worry, and I am not alone, that the Insurance Capital Standard, or the ICS, currently being developed by the International Association of Insurance Supervisors is incompatible with the U.S. insurance market. There is widespread concern that the ICS is too sensitive to short-term fluctuations in market and certain asset categories and does not take into account certain aspects of the assets that insurers hold. The result is that the implementation of ICS in its current form would harm the availability of long-term insurance products that Americans rely on for financial security. Our U.S. representatives at IAIS need to make sure that ICS works for the U.S. market and by not allowing the proposal to go forward until it does.

Next, I would like to touch on some troubling efforts to use our financial system to address climate change. Now some liberal activists want to pressure insurance companies and other financial institutions to deny services to traditional energy companies and other carbon-intensive industries. Such efforts are profoundly misguided.

Addressing the difficult challenges posed by global warming requires political decisions involving important tradeoffs, and we have seen those tradeoffs in action in recent months: soaring energy prices; European Nations have made plans to reopen coal power plants and extend the lives of nuclear plants; likewise, in the U.S., we have seen the Biden administration's hostility to new energy production contribute to shockingly high gasoline prices. That is a painful consequence of policy choices.

In a democratic society, those choices and the tradeoffs associated with them must be made by elected representatives who are accountable to the American people, not unelected activities, bureaucrats, or insurance executives, for that matter.

To be sure, insurers face financial risks in the form of natural disasters. After all, it is a core business of the property and casualty insurance industry. Insurers must be allowed to set premiums that accurately reflect these risks, and to the extent that climate change exacerbates these risks, then they are going to need to adjust their prices accordingly. Higher premiums are an important signal to policyholders that warn of increased risks of fire or flood or earthquakes or other peril. Further, they create a financial incentive to mitigate risk, which leads to safer and more resilient communities and society.

The bottom line is that a well-functioning insurance industry is quite capable of addressing the natural disaster risks that it faces today and in the future.

I would also like to address plans to create a federally guaranteed pandemic risk insurance program. As proposed, this program would be akin to the Terrorism Risk Insurance Program, or TRIA. As a reminder, TRIA mandates that insurers offer terrorism insurance and in the event of an attack the Federal Government bears an increasingly share of the cost of claims depending on the severity.

Well, a similar program for pandemics would be very, very problematic. First of all, it is hard to imagine that insurers are well equipped to quickly distribute hundreds of billions or maybe even trillions of Federal dollars. Recall that in a matter of months the Paycheck Protection Program distributed over half-a-trillion dollars via the banking system, but banks and other financial institutions participated on a voluntary basis. Compare that to the disastrous claims processing after Superstorm Sandy.

But more importantly, a federally guaranteed pandemic risk insurance program would encourage State and local governments to impose economically devastating shutdowns in the future. Such a program would in fact incentivize State and local policymakers to quickly impose lockdowns with their jurisdictions with the assurance that the Federal Government risk insurance program will bail them out. Instead of considering policies that will facilitate future lockdowns that repeat the mistakes of the past, we should be

thinking about future mitigation measures that do not crush business, workers, and the economy, and do not harm our children's educations.

Let me conclude with this observation. A well-functioning insurance industry is a critical component of economic prosperity and financial security for all Americans. Everyone will be better off if we resist activists' efforts to use insurance as a tool to pursue social policy goals. Insurance is not a legitimate tool, as some have suggested, to decarbonize the economy, to infringe on Second Amendment rights of law abiding citizens, or to mitigate wealth inequality. Let us have insurers stick to the business of insurance.

I look forward to discussing these issues today.

Chairman BROWN. Thank you, Senator Toomey.

I will introduce today's witnesses, and then they will begin their testimonies. The Honorable Kathleen Birrane is the Maryland Insurance Commissioner testifying on behalf of NAIC. She previously was a partner at DLA Piper and Principal Counsel for the Maryland Insurance Administration at the Maryland Office of the Attorney General.

Mr. Steven Seitz is Director of FIO at Treasury. He joined FIO as Deputy Director, previously worked at the Office of the Assistant General Counsel at Treasury and the CFTC.

Welcome to both of you.

Commissioner, please begin your testimony. Thank you.

**STATEMENT OF KATHLEEN A. BIRRANE, MARYLAND INSURANCE COMMISSIONER, ON BEHALF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS**

Ms. BIRRANE. Chairman Brown, Ranking Member Toomey, Members of the Committee, thank you for the invitation to testify today. I will use my time today to touch briefly on several issues we know are of interest to Members of the Committee.

First, we have been actively monitoring the growth in private equity-owned insurance. Our solvency framework includes significant checks and balances to protect policyholders, including public disclosures, capital requirements, and conservative accounting requirements which are used to assess all risks to insurers regardless of the type of ownership. As insurers of all types are searching for investment yield to avoid raising prices, insurance regulators are reviewing existing guidelines and considering new requirements to ensure our ability to assess and address the risks to policyholders.

The NAIC is working through 13 regulatory considerations applicable to both private equity-owned insurers and other insurers with similar features. We have extensive data reporting and analytical capabilities to review and assess alternative investments or unique structures and are continuing to refine those tools. We are confident in our system to appropriately oversee insurers no matter how they are structured, and we will certainly keep the Committee apprised of our work in that regard.

Next, insurance regulators also recognize the importance of cybersecurity risk management and continue to upgrade data security safeguards. The NAIC Insurance Data Security Model Law updates regulatory requirements relating to data security, the investigation of a cyber event, and the notification to State insurance

commissioners of cyber events. States continue to adopt the model, which now covers 83 percent of the market as measured by gross written premium.

The NAIC also created a new Innovation, Cybersecurity, and Technology (H) Committee, which I chair, to address the insurance implications of emerging technologies and cybersecurity and to ensure coordination and consistency among insurance regulators.

The NAIC also continues to facilitate tabletop exercises with insurers, regulators, and law enforcement to explore cyber incident response.

Another top priority is climate risk and resilience. This year, the NAIC facilitated revisions to its Climate Risk Disclosure Survey which is now aligned to the FSB's TCFD. These disclosures, now covering 80 percent of the market by premium, help insurance regulators assess insurance industry risks and actions to mitigate climate risk.

We also monitor insurers' ability to pay claims following catastrophic events. We recently recommended that wildfires be explicitly added to the Risk-Based capital framework for catastrophe risk exposure. Further, the NAIC is creating a Catastrophe Model Center of Excellence to provide insurance regulators with access to information and training on catastrophe models.

Another area of activity for State insurance regulators is the intersection of race and insurance. The NAIC's work focuses on evaluating issues of race and diversity within the sector and addressing market access and potential barriers. Additionally, the NAIC formed a New Avenues in Insurance Careers Foundation to help foster interest in the insurance careers with a focus on students from underserved and diverse communities.

Turning to the international front, State insurance regulators continue to engage on a variety of issues including the IAIS's development of an Insurance Capital Standard. The NAIC, along with our Team USA partners, including FIO, have been clear that the ICS does not work for the U.S. market or our supervisory regime and therefore has developed an aggregation method as a comparable to the ICS. We will continue to advocate for recognition of the U.S. approach to group capital within the IAIS and as already reflected in covered agreements between the U.S. and the EU and U.K.

Finally, we would like to highlight a few of our Federal priorities. We urge Congress to pass a long-term NFIP reauthorization that encourages investment in flood mitigation efforts, and we support Senator Scott's Primary Regulators of Insurance Vote Act which would provide State insurance regulators with a vote on FSOC. We are also working on legislation to help protect policyholders during an insurance receivership.

So thank you again for the opportunity to testify, and I am pleased to take any of your questions.

Chairman BROWN. Thank you, Commissioner. Director.

**STATEMENT OF STEVEN SEITZ, DIRECTOR, FEDERAL INSURANCE OFFICE, U.S. DEPARTMENT OF THE TREASURY**

Mr. SEITZ. Chairman Brown, Ranking Member Toomey, and Members of the Committee, thank you for the opportunity to testify

today about current issues in insurance. I am the Director of the Federal Insurance Office within the U.S. Treasury Department. I would like to begin by briefly outlining FIO's role and responsibilities and by describing some of our current priorities.

The United States is the world's largest insurance market, and its insurers provide a diverse range of products to support the needs of consumers and businesses in the United States. The U.S. system of insurance regulation is primarily State-based. However, FIO has a significant role to play as reflected in its statutory duties and authorities. FIO advises the Treasury Secretary on major domestic and prudential international insurance policy issues, develops Federal policy on international insurance issues including representing the U.S. at the International Association of Insurance Supervisors, administers the Terrorism Risk Insurance Program, monitors the extent to which traditionally underserved communities and consumers have access to affordable insurance products, assists the Secretary in negotiating covered agreements with foreign jurisdictions, and monitors the insurance sector, including identifying issues or gaps in the regulation of insurers that could contribute to a systemic crisis. As FIO's Director, I also serve as a nonvoting member of the Financial Stability Oversight Council. These authorities reflect the need for FIO to provide a national Federal perspective in this critical area.

I would like to highlight five current FIO priorities.

Climate-related financial risk is a top priority for our office. We are focused on three areas which are consistent with President Biden's Executive Order on Climate-Related Financial risk. First, FIO plans to publish a report assessing climate related issues and gaps in the supervision and regulation of insurers. Second, FIO is evaluating the potential for major disruptions of private insurance coverage in U.S. markets that are particularly vulnerable to the effects of climate change. Third, we are increasing our engagement, both domestically and internationally, on climate-related financial risk issues. As we move forward with these efforts, we will also seek consistent, comparable, and granular data to increase our understanding of the risks from climate change to policyholders, insurers, and the financial system.

A second focus area for the Federal Insurance Office is the growing role of alternative asset managers, such as private equity firms, in the U.S. insurance sector. This evolution is one that our office has highlighted for several years. It warrants increased attention to ensure that regulatory mechanisms are appropriately designed to address the activities and market developments that we outlined in our recent letter to Chairman Brown. We encourage continued focus and increased progress by State regulators in this area.

FIO will continue to prioritize four areas of research and action on this topic: first, liquidity risk; second, credit risk and capital adequacy; third, offshore reinsurance implications including the increased interconnectedness between the U.S. and Bermuda insurance markets; and fourth, potential conflicts of interest.

FIO is also focused on cyber-related risk which is a top priority for Treasury and the entire Federal Government. FIO has been examining insurers' own cyber resilience as well as the development of the cyber insurance market. We have increased our data collec-

tion in this area with regard to the Terrorism Risk Insurance Program and have supported the development of Treasury's counter-ransomware strategy. We are also working with the DHS's Cybersecurity and Infrastructure Security Agency in connection with GAO's recommendation that we jointly assess the need for a Federal backstop for cyber insurance. FIO is also coordinating closely with the White House Office of the National Cyber Director on these issues.

A fourth priority for FIO is our representation of the United States at the IAIS in close coordination with the NAIC, the States, and the Federal Reserve. In addition to its focus on climate, private equity, and cyber, the IAIS is also considering other important topics such as the development of the Insurance Capital Standard and the related comparability work involving the aggregation method as well as the implementation of the holistic framework for the assessment and mitigation of systemic risk. These topics are important global initiatives that will affect the U.S. insurance sector, and it is critical for FIO and the United States to remain engaged at the IAIS on these issues.

Fifth and finally, FIO is prioritizing its work on diversity, equity, and inclusion. Consistent with our statutory authorities, FIO looks at these issues through the lens of the availability and affordability of insurance products, particularly for traditionally underserved consumers and communities. Right now, we are working to update our study on personal auto insurance affordability. Additionally, these issues are also key components of our upcoming climate work.

On all these topics and many others, FIO values our close relationship and frequent coordination with State regulators, the NAIC, our Federal partners, and international counterparts as well as with insurance industry stakeholders.

Thank you again for the opportunity to testify today.

Chairman BROWN. Thank you, Director. Thank you, Director, for FIO's response to my letter earlier this year about private equity's growing role in the insurance sector. You mentioned that once a company transfers its pension obligations in a pension risk transfer the PBGC guaranty no longer applies; participants would lose protections under risk. You reemphasized that. Thank you.

What new problems—two questions: What new problems arise from these practices where pensions are transferred to life insurers, and how do they pose risks to workers without ERISA and PBGC protections, and do you have—I guess three questions. Do you have additional concerns for the broader financial system, its impact?

Mr. SEITZ. No. Thank you, Senator Brown, for that question. We share your interest in the importance of this topic. The U.S. insurance sector, and particularly the life and retirement sector, is critical for millions of working Americans that are relying on these products for their retirement security.

In our letter, we highlighted the four key areas that we are focused on: First, enhancing FIO's monitoring of the potential liquidity risk of the entire life insurance sector but also particularly related to PE-owned insurers. Second, we are looking at regulatory mechanisms and whether they are appropriately designed for

issues related to credit risk and capital adequacy to accommodate and appropriately regulate this type of business model. Third, we are also looking at the offshore reinsurance implications, particularly the increased interconnectedness between Bermuda and the U.S. markets where certain blocks of business are being transferred offshore. And, fourth, we are also looking at potential conflicts of interest.

These are important issues for our topic, and we will be working closely with the NAIC and the States on their focus going forward and look forward to further updating this Committee as that work progresses.

Chairman BROWN. Thank you, and we will ask for that. My interest in this issue has increased in part because Congress just worked a year ago—I mean, worked for several years and was able to fix problems in the multi-employer pension system. We know the human costs that failing pensions pose to workers who earn these benefits and who have that expectation through a lifetime of work.

Congress established, as you know, in a bipartisan way, PBGC and passed ERISA. It is imperative that insurers—and we are counting on both of you on this to ensure—it is imperative that insurers not be allowed to do an end run around the system established to protect pensioners.

Commissioner Birrane, thank you again for being here. I have heard from nonprofit associations reaching out to the State insurance commissioners and NAIC about difficulties finding and affording property and casualty insurance. My question is this: What are the tools available for State insurance commissioners to solve this market failure? And it is a market failure.

Ms. BIRrane. So thank you, Senator Brown, for the opportunity. As you know, the NAIC has long opposed the expansion of the Liability Risk Retention Act to allow RRGs to write commercial property insurance. It is our sense that commercial property insurance is generally widely available, and we have serious concerns that nonprofits that are already vulnerable could be put at greater risk from a consumer protection standpoint if they are allowed to purchase their property insurance from an entity that is not subject to the same rigorous standards and multistate enforcement as admitted carriers, which really creates an uneven playing field.

Most States have a residual market for property insurance, including commercial property insurance. I know in my State I have queried our nonprofits and this is not an issue that we see in at least the State of Maryland. Other commissioners across the country are making similar efforts to look at their markets to see where issues exist, and we would be happy to know about specific circumstances and make ourselves available to work with nonprofits that are having difficulty getting commercial property insurance.

Chairman BROWN. OK. Your assessment differs a bit from ours. It is a serious problem that has not been solved in the marketplace. In the past, when faced with similar market issues that span the country, Congress passed the Liability Risk Retention Act. As you know, I am working to amend the LRRRA to narrowly address this issue of affecting community-based nonprofits.

Director Seitz, are you concerned about this gap in the market in ensuring nonprofits have access to the insurance they need?

Mr. SEITZ. No. Thank you for that question. It is an issue that we have also been tracking, as Commissioner Birrane mentioned. It is an area we have been engaging with various stakeholders on the topic with regard to their ability to get coverage. I think we will look forward to working with the NAIC and your team as we look into this issue in more depth.

Chairman BROWN. OK. And count on us to do that. We have been working with NAIC to find a solution. Risk Retention Groups are regulated by State insurance commissioners under NAIC regulations.

And, Commissioner, I just wanted to ask again, can we work together to find a solution that responsibly increases insurance capacity for RRGs to address this problem?

Ms. BIRRANE. We absolutely want to work together for a constructive solution for nonprofits who need commercial property insurance, and we are happy to work with you and your staff and with FIO.

Chairman BROWN. Thank you. Count on us for that.

And I wanted to ask a third question—I will not take time. My 5 minutes is up—about climate catastrophe risk, and we will submit something in writing or maybe as part of a second round, or my colleagues, probably one of them will ask something about that.

So, Senator Toomey.

Senator TOOMEY. Thank you, Mr. Chairman.

The Chairman brought up the circumstances that occur occasionally where a pension risk transfer occurs, and my understanding is the nature of this, what we are talking about here, is when a company has a defined benefit obligation to its retirees. It can purchase an annuity, essentially, from an insurance company, which then transfers the management of this to an insurance company.

And, as the Chairman pointed out, in that scenario, it is my understanding that the PBGC guaranty no longer applies. However, there are insurance funds. There are insurance guaranty funds.

And so, Ms. Birrane, would I be correct in assuming that the insurance guaranty funds in the various States would be there as a backstop to the ability of the insurance companies to honor their contractual obligation to make those payments?

Ms. BIRRANE. Yes, Senator, that is correct.

Senator TOOMEY. And the transfer itself—so after the transfer occurs, ERISA no longer applies is my understanding, but the mechanism of the transfer itself is regulated by ERISA. Isn't that true?

Ms. BIRRANE. That is correct. ERISA no longer applies to the entity that now bears the risk—

Senator TOOMEY. Right.

Ms. BIRRANE. —because what has really happened is that the pension fund is buying an insurance product—

Senator TOOMEY. Right.

Ms. BIRRANE. —in order to meet those obligations.

Senator TOOMEY. Right. So then it raises an interesting question like in your experience, Ms. Birrane, I would guess that you would probably agree with me that insurance companies, especially like life insurance companies, have extensive experience in managing long-term liabilities like that is what they do. So the idea of wheth-

er they are in a good position to manage the long-term liabilities of a defined benefit pension plan suggests to me like they are likely to be very well suited for managing that task. Is that your sense?

Ms. BIRRANE. I would agree, and I would also point out that they are subject to rigorous financial reporting and oversight and life insurance annuity contracts are protected by the State guaranty funds—

Senator TOOMEY. Right.

Ms. BIRRANE. —which have themselves noted that insurance regulators hold life insurance companies to much stricter standards and more intensive oversight than are applied by pension regulations to the pension funds themselves.

Senator TOOMEY. Right. Now all those rigorous regulations and supervision that you just alluded to, that does not go away if the insurance company happens to be owned by a private equity firm, does it?

Ms. BIRRANE. No, absolutely not. If anything, private equity funds tend to be subject to stricter regulation.

Senator TOOMEY. Thank you.

Director Seitz, it has come to my attention that there is work being done on an internal briefing memorandum regarding private equity involvement in insurance, and I am not—you may be involved in that for the international—I lose track of my acronyms here, but it is the IAIS. Is that true? Is there such a memo being in the works?

Mr. SEITZ. With regard to the International Association of Insurance Supervisors—

Senator TOOMEY. Right, that is it.

Mr. SEITZ. —they have discussed the topic of private equity, including at its last year's annual conference there was a panel discussion on that. And it is, I think—you know, I cannot disclose the private conversations at the IAIS, but obviously, it is one of the themes that we are seeing in the macroprudential work being done at the IAIS.

Senator TOOMEY. So are you involved in an effort to make recommendations to the IAIS regarding private equity's involvement in insurance?

Mr. SEITZ. As part of our work at the IAIS, we are closely coordinating with the Federal Reserve—

Senator TOOMEY. Yeah.

Mr. SEITZ. —the NAIC, and the U.S. States on a variety of issues including work related to the capital standards and also regarding the holistic framework which the NAIC is adopting.

Senator TOOMEY. OK, but you did not answer my question. Are you personally involved in research or development of a memo or an analysis that will include policy recommendations to the IAIS regarding private equity in insurance?

Mr. SEITZ. You know, our teams are working closely with the NAIC and the States. You know, I am a member of the executive committee, and there are a variety of topics that the IAIS is discussing, and one of those topics at our upcoming meetings will be private equity.

Senator TOOMEY. Yeah, so you are obviously trying to evade my question. I do not know why it is such a difficult question to an-

swer. Let me try it a different way. If there is a memo or a piece of research work that is done and you are involved in it and it is submitted to the IAIS, do you intend to share that with the Committee?

Mr. SEITZ. You know, I think similar to the IAIS we value the importance of transparency at the IAIS, and we would work with our State and Federal partners at the IAIS to make sure that there is appropriate transparency. And, this will be a topic that we will likely include in our upcoming report to this Committee that is issued with the Federal Reserve Board regarding our activities in international supervisory forms.

Senator TOOMEY. I see I am out of time, Mr. Chairman.

Chairman BROWN. Thank you, Senator Toomey.

Senator Reed from Rhode Island is recognized.

Senator REED. Thank you, Mr. Chairman, and thank you, Madam Commissioner and Director.

In May 2021, GAO released a study about challenges that insurers and policyholders face in an evolving market for cyber insurance. Director Seitz, can you explain the key challenges that GAO identified with respect to pricing cyber insurance and ensuring that policies provide appropriate coverage?

Mr. SEITZ. No. Thank you, Senator, for your question on that topic. We have closely reviewed the GAO study and contributed to it, and we agree with the conclusions in that study, I think, in particular, looking at some of the pricing challenges and price increases that have been happening for the sector. Additionally, you are seeing some of the carriers withdraw coverage from certain parts of the market.

I think, in particular, an area of focus for our office as we administer the Terrorism Risk Insurance Program is the extent to which cyber coverage is available to small and medium enterprises. I think, in particular, we have collected information for the first time last year regarding the extent to which SMEs can access that coverage, and that is going to be a priority of our work going forward and additionally an aspect of the work that we are doing with CISA regarding the catastrophic backstop for cyber insurance.

Senator REED. At this point, just for clarification, terrorism insurance, would that include cyberattacks or is that sort of a function of the type and degree of the attack?

Mr. SEITZ. The Terrorism Risk Insurance Program does cover cyber insurance written in the TRIP-eligible lines of insurance, and with regard to our work in that area it is an issue that we have discussed extensively in our prior reports, particularly looking at how the certification provisions under TRIA would apply to cyber events when you are looking at issues of attribution and elsewhere.

Senator REED. Thank you.

Commissioner Birrane and Director Seitz, how are NAIC and FIO, respectively, working with the insurance industry to address these challenges of cyber insurance? And every day there seems to be a new, dramatic challenge presented by cyber or something, so this is the beginning, not the end, of our discussion. Madam?

Ms. BIRANE. Thank you, Senator. I would say with respect to the NAIC the first thing that we have done is develop a cybersecurity supplement by insurers—for insurers' annual statements so

that we can track very closely and gather information about insurers who are writing cyber insurance coverage in the U.S. We utilize the data that we have captured within this cyber supplement to monitor the risk and monitor what is happening in the market.

I think what we can confirm is that between 2020 and 2021 there was an increase of approximately 75 percent in direct written premium, but it is very clear that that growth was due primarily to pricing increases rather than additional coverages. And so our data confirms that along with an increase in the frequency and the severity of cyberattacks, and the number of cyber claims that are continuing to increase, premiums are going up, limits are going down. It is a much harder underwriting environment.

I would say with respect to the market as a whole we are actively engaged in efforts to look at what is the appropriate backstop, how do we make sure that there is a robust financing mechanism available, even with—even in the event that the insurance market does not have the appetite to cover all of it.

Senator REED. Director Seitz, any comments?

Mr. SEITZ. No. I think Commissioner Birrane said it well. Thank you.

Senator REED. Commissioner, you clearly point out the increasing prices of cyber insurance, which obviously affect every business, particularly small businesses and municipalities. And what steps can the State regulators take to try to reduce those premiums and ensure coverage is available?

Ms. BIRRANE. So insurance is fundamentally based on risk, so pricing is based on risk. And insurers engage in risk-based pricing; that is what we expect them to do. And so as risks increase, so do premiums and costs.

We have switches that we can toggle in terms of opening up markets like the surplus lines market or captive arrangements for certain companies and certain circumstances, but at some point there are risks that are very high. They are either too large or they are too volatile or they are too certain to be able to be as affordable as we would like them to be.

I would point out that what we see happening in the market, in the tightening of the market, the increasing costs, and the increasing underwriting standards also creates a discipline. It also helps with good cyber hygiene. So part of what it does is it asks businesses to themselves be more responsible in terms of taking their cybersecurity risks seriously, and as companies pair with insurers to do that and mitigate and reduce their risk, then that allows their programs to be more affordable.

Senator REED. Thank you very much.

Thank you, Mr. Chairman.

Chairman BROWN. Thank you, Senator Reed.

Senator Rounds of South Dakota is recognized.

Senator ROUNDS. Thank you, Mr. Chairman, and thank you to both of you for being here with us today.

As you are both aware, in response to the development of the proposed International Capital Standard, Team U.S.A. proposed the aggregation method as an alternative framework. However, comments filed in response to a recent IAIS consultation on the proposed criteria to determine the comparability of AM and ICS in-

dicates that the current process may very well be biased toward the ICS and will likely preclude a finding of comparability for AM which we use or which we want.

Could each of you just take a minute and explain why a Eurocentric capital model would have a negative impact on consumers' access to U.S. insurance products? I am assuming that both of you feel that that may be the case. I would begin with Commissioner Birrane.

Ms. BIRRANE. Sure. Thank you, Senator, for the question. So the U.S. market includes a number of foreign-owned insurers with U.S. businesses. So comparability would allow a foreign jurisdiction to defer to U.S. capital requirements for that business, so it encourages that business. Additionally, as U.S.-based insurers seek to operate abroad, it is important that those countries recognize relevant aspects of our system.

I would also just point out that the covered agreements between the U.S. and the EU and U.K., along with our qualified jurisdiction process, already require recognition of U.S. group capital. So the IAIS process should really not seek to contradict that recognition.

Senator ROUNDS. Thank you.

Director Seitz? And I made the assumption, but I am assuming that you are in agreement with my statement that we really want to maintain the current aggregated proposal that we use in the United States today.

Mr. SEITZ. No. Thank you, Senator, for your question on this issue. It is one that is critically important for the U.S. insurance sector, and it is one that our team has been working on for the last several years in close coordination with the NAIC, the States, and the Federal Reserve. We believe it is critical that we remain engaged in this conversation for many of the reasons that you noted. In particular, the international community is moving ahead with the development of the Insurance Capital Standard, and we need to be at the table to improve that methodology so that it is more compatible with our U.S. system.

As we discussed earlier, you know, the ICS does not appropriately reflect certain aspects of our regime, particularly for those long-dated, long-duration products which are critical for millions of Americans entering retirement. And I know that will be a priority issue for us over the coming months, and we look forward to working with the States, the NAIC, and the Fed as we take this important work forward.

Senator ROUNDS. Thank you. I really do believe that the U.S. system of State-based insurance regulation is truly the gold standard when it comes to protecting our insurance markets and the insurance consumers in my home State of South Dakota and across the country.

Commissioner Birrane, do you believe that our State-based regulatory system has been effective and successful?

Ms. BIRRANE. Very much so. I think it was interesting, you know, as Senator Brown referred to AIG. And I think that for those of us that lived through that period of time and, you know, the crash of the capital markets in 2008, what we know is that the one set of companies that did extremely well were the insurance companies, the P&C carriers that were regulated by the States. So as AIG

sought to recover, it was those companies, those assets, they were able to sell in order to fund that recovery.

So where State regulation is in place I think we have demonstrated effectiveness over time. We talk about life insurance companies, and we talk about the safety of life insurance companies. The insolvency of a life insurance company is almost unheard of, and the notion that policyholders in those rare instances where there has been an insolvency are not getting paid is also unheard of.

So I think that what the State-based regulatory system has proven over and over and over again, you know, having just come through a pandemic, having just come through a very difficult environment, having all of the things that are going on in our society right now, and yet the State insurance system is protecting policyholders, claims are being paid. And so I think that it is infinitely clear that the mechanisms that exist at the State-based level are able to protect policyholders and respond quickly and nimbly to changes in circumstances that warrant additional adjustments in how we regulate.

Senator ROUNDS. Well, Commissioner Birrane, look, I could not agree with you more, and I really do believe that Congress should allow you and the NAIC to do your job. And I think it is imperative that Congress recognizes that it has worked successfully and that when we start talking about the other items that are critical—and one of the items on it is private equity—there are some very good messages out there about what private equity has done for the insurance markets in the United States as well.

My time is expired, but I thank you for being—I thank you both here for your answers today.

Thank you, Mr. Chairman.

Chairman BROWN. Thank you, Senator Rounds.

Senator Menendez is recognized from his home or his office. I do not know where he is. Senator Menendez, remote.

Senator MENENDEZ. Thank you, Mr. Chairman.

Last year, I introduced the Clarifying Law Around Insurance of Marijuana Act, or the CLAIM Act, to provide a safe harbor for insurers to provide products and services to businesses that are involved with State-legalized cannabis without the risk of Federal prosecution. This bipartisan legislation was included as a provision of the SAFE Banking Act, which I strongly support.

Commissioner Birrane, can you please describe why we need the SAFE Banking Act enacted as soon as possible?

Ms. BIRRANE. Thank you, Senator. As you know, the NAIC does support the SAFE Banking Act. Insurance regulators recognize State-legalized cannabis businesses require access to insurance to mitigate the risks that they face like any other authorized business. The SAFE Banking Act would help remove Federal barriers for insurers to insure State-legalized cannabis businesses. You know, it is really critical that businesses be able to buy insurance, that they be able to pay for that insurance, and when claims occur, that insurance companies be able to use the banking system to pay those claims. The SAFE Banking Act would allow that to happen.

Senator MENENDEZ. Thank you. I am concerned that businesses that have nothing to do with cannabis could face serious con-

sequences if the bill is not enacted. Imagine a scenario where a New Jersey lightbulb manufacturer sells a product to a State-legalized cannabis business and there is a fire related to the lightbulb, causing the business to suffer loss. Under current law, in the scenario I just described, could the lightbulb manufacturer's insurance company face Federal charges if they pay the claim?

Ms. BIRRANE. So the challenges that insurance companies have is using the banking system to transfer funds to a cannabis business. So the answer is that there is a circumstance which could be challenging for the lightbulb company's insurer in trying to use the banking system to pay money to the cannabis business.

Senator MENENDEZ. Well, the House has passed this bipartisan measure seven times, and I think it is long past for the Senate to do the same.

Let me turn to pandemic risk insurance. When COVID-19 first hit our country in 2020, small business owners discovered that most business interruption policies excluded claims from viral contamination, disease, or pandemic, leaving many businesses without relief. Instead, Congress quickly provided on a bipartisan basis trillions of dollars in aid to help keep small businesses afloat and save jobs. I am proud I voted for the American Rescue Plan, which was critical to our COVID response, but we should be planning ahead to get—to better protect our economy from the risk of a new pandemic that could threaten to overwhelm the health system. In today's interconnected world, the question of the next pandemic is not if, but when.

Commissioner Birrane, is there still limited pandemic business interruption coverage in the market?

Ms. BIRRANE. Yes, I would say that the scope of coverage that is available in the market has certainly not changed; it certainly has not expanded.

Senator MENENDEZ. So wouldn't business owners, employees, and the Federal Government be better prepared for the next pandemic if Congress established a public-private insurance solution to provide coverage for pandemic-related losses?

Ms. BIRRANE. I think that business interruption insurance in a circumstance like this is an area where the risk is potentially so large and so uncertain that it is not going to be covered by the private insurance market and in those circumstances it is certainly appropriate to discuss what public-private partnerships could do in order to make sure that financing is available in those extraordinary, catastrophic circumstances.

Senator MENENDEZ. Well, I appreciate that. It is critical that we plan ahead for the next pandemic rather than wait until the next outbreak of a new deadly virus, and far from incentivizing lockdowns, what we really need is to find a way to incentivize businesses to preserve the lessons of COVID and accept a level of personal responsibility if they are unwilling to do so.

And similarly, I do not know those who would simply wait until a crisis point and have the Federal Government distribute trillions of dollars instead of working ahead of time to develop a more targeted response to the specific needs of an individual business. That is what I think we should do.

Finally, Mr. Chairman, last month, FEMA reported that over 425,000 policyholders dropped out of the National Flood Insurance Program since Risk Rating 2.0 took effect. That is nearly 10 percent of the program. FEMA originally estimated in a pessimistic model that 20 percent of the policyholders would drop coverage over 10 years. The Agency predicted it would take years for 425,000 policyholders to drop coverage, but instead, it took 8 short months. A majority of homeowners across the country are already uninsured against flooding, and it is clear that Risk Rating 2.0 is only making the situation worse.

I think FEMA has misled us, and I want to work with you, Mr. Chairman, to advance the bipartisan legislation we have before the problem gets even worse.

Chairman BROWN. Thank you, Senator Menendez.

Senator Tester from Montana is recognized.

Senator TESTER. Yeah, thank you, Mr. Chairman, and I want to thank both the folks that are here in front of us today for testifying.

And I want to touch back on cyber a little bit.

Commissioner, is there anything that Washington, DC, Congress or the executive branch, needs to do to deal with cyber from your industry perspective or are we OK where we are at?

Ms. BIRRANE. So, Senator, are you speaking in terms of the protection gap?

Senator TESTER. I am speaking in terms of the threat, and I will get into the increase in premiums due to cyber. Is there anything we need to be doing to put forth some relief? I am not talking about writing checks out to people. I am talking about making policies that will make cyber more manageable. Cyber threats.

Ms. BIRRANE. Sure. So I think from the perspective of our industry we are looking at assuring that there are adequate controls in the insurance industry so that they can withstand potential cyber threats. What the NAIC has been engaged in is, of course, we have developed a model law which States continue to adopt. Now 83 percent of the market has adopted or are subject to those laws, which improve and increase the security of data and the rapidness of notice to insurance commissioners about when there has been a data incident. We continue to strengthen and update our guidance for financial examiners.

Senator TESTER. But, so what I am hearing you say is that between NAIC and the State governments that the issue is being handled adequately.

Ms. BIRRANE. We believe that we have an adequate framework in place to assure that insurance companies—

Senator TESTER. OK.

Ms. BIRRANE. —and insurance data is protected.

Senator TESTER. OK. You will have to correct me if I did not catch this right, but when Senator Reed was asking questions you said there was a 75 percent increase in premiums due to cyber?

Ms. BIRRANE. Right. So on the one hand, we talk about what insurance companies are doing to make their data safe.

Senator TESTER. Yeah.

Ms. BIRRANE. When we talk about then insurance companies as risk financiers—

Senator TESTER. Yes.

Ms. BIRRANE. —so when they sell policies—

Senator TESTER. Yeah.

Ms. BIRRANE. —policies have certainly become more expensive for the businesses that buy those policies.

Senator TESTER. And that is taking what kind of timeframe, the 75 percent increase?

Ms. BIRRANE. That is over about the course of a year.

Senator TESTER. One year.

Ms. BIRRANE. One year.

Senator TESTER. Do you—the Ranking Member talked about you guys dealing with risk, long-term, short-term. Have you guys done that with issues around climate? Let me give you an example. Where I live in Montana—it is a big State, but where I live in Montana it is dry as hell. A few months ago, you probably heard about the flood that came out over Yellowstone Park that was a 500-year event. It seems like we are having 500-year events and 100-year events every decade. So do you guys take that into account?

Ms. BIRRANE. So we certainly track very closely the frequency and the severity of perils—

Senator TESTER. Yes.

Ms. BIRRANE. —and claims. So for example, in the world—

Senator TESTER. Yeah, go ahead. Keep going, real quickly.

Ms. BIRRANE. I was going to say, in the world of climate—

Senator TESTER. Yeah.

Ms. BIRRANE. —specifically, we know that weather patterns are changing and that those weather patterns are causing increased—

Senator TESTER. Yeah.

Ms. BIRRANE. —claims activity, et cetera.

Senator TESTER. No doubt about that. Can you give me any kind of an idea, just from a property damage standpoint, what the increase in premiums has been because of that?

Ms. BIRRANE. I have to tell you I do not have the numbers at my fingertips, and I am happy to follow up to give you those numbers, but the increases are exponential. So we are seeing much, much larger numbers of claims. You know, weather events are more frequent. They are more severe and—

Senator TESTER. I would love to get those numbers—

Ms. BIRRANE. Absolutely.

Senator TESTER. —because there are a number of folks in the body, in Congress, that think ignoring climate is something that will make it go away when in fact my experience on a farm in north central Montana is it ain't going away. It is, in fact, getting far worse. I mean, last year was the worst crop we ever cut. This year was the second worst crop we ever cut. And I know I look very young, but we have been on the farm for 45 years. So it is pretty insane.

I want to talk really, really quickly about NARAB. This is the damndest thing I have ever seen because we passed a bill years ago and, quite frankly, we still do not have a board, did not have it through Obama, did not have it through Trump. Number one, could you just give me the benefits of that NARAB board?

Ms. BIRRANE. So I feel like that is an issue that we would probably do better briefing you on afterwards in terms of the board, but you know, the NAIC's position has been that the board should be created and established.

Senator TESTER. Can you give me any update on—Director Seitz, give me any update on the status of that NARAB board being fully functional?

Mr. SEITZ. No. Thank you for that question. We share recognizing the importance of NARAB. And it is an issue that we have been meeting with a variety of stakeholders on, particularly on the broker community, to sort of think through that process again, and it is an issue that we have been focused on for the last few years in our office, of trying to move that forward.

Senator TESTER. Well, and I am way out of time, but I would just say, please be aggressive. You know, bounce some people around. Do whatever you got to do. Get this damned thing done. It would be, I think, a win for the consumer, a win for the industry, and a win for the Administration. Thank you.

Thank you, Mr. Chairman.

Chairman BROWN. Thank you, Senator Tester.

Senator Hagerty of Tennessee is recognized.

Senator HAGERTY. Thank you, Mr. Chairman, Ranking Member Toomey. Thank you both, and to our guests, thank you for being here today.

Commissioner Birrane, I would like to turn first to you. There have been a number of concerns raised about the lack of regulation and transparency with respect to private equity backed insurers. I would like to talk with you from a State regulatory standpoint. My question is: Are insurers that are affiliated with private equity firms treated any differently than other insurers, and are they somehow able to avoid oversight at the State level?

Ms. BIRRANE. No, Senator, private equity-owned insurers are not treated any differently than other insurers except to the extent that it has been the—common practice since about 2013 that States have actually imposed greater requirements on PE firms that purchase insurers. So they have generally been required to accept additional conditions and reporting obligation as a condition of the approval of their investments and their investment in an insurance company. So those stipulations are now part of the financial analysis handbook that States use when they assess a request by any entity to purchase an insurance company.

I would also say that more recently, in light of an increase in PE ownership in life insurers and the complexity of some of their investments, and investments not just made by PE owned insurers but by life insurers generally, the NAIC's Macroprudential Working Group has constructed a list of 13 specific regulatory considerations that are focused on investment disclosures, ownership and collateral, reliance on rating agencies, fees, and pension-risk transfer guidance.

Senator HAGERTY. I want to come to pension-risk transfer in just a minute, but I want to be clear. Again, you said that there are actually additional regulations, an additional layer of regulations, in place for private equity-owned insurers at the State level.

Ms. BIRRANE. That has been the standard that has been employed by most States.

Senator HAGERTY. Thank you. Back to pension-risk transfers, that is another topic I wanted to discuss with you. That is the process by which a corporation might transfer its pension risk to insurance companies. What tools do State insurance regulators have to ensure the protection of policyholders in that instance, and are they any less safe once the pension has been moved to an entity that is regulated by the State insurance regulatory system?

Ms. BIRRANE. So the insurance regulators have a very robust set of tools because we are the primary regulators of the financial solvency of insurance companies and our system is designed to avoid failure. Our system is designed to have tremendous optics into the financial standing of those companies. We use a variety of tools to assure that companies maintain the reserves that they need, particularly with life insurers that have very long-term risk. So there are annuity obligations; there are life insurance obligations, to assure that they are adequately reserved.

So we have all of those systems in place. The fact that a PE company owns that insurance company does not change any of that.

Senator HAGERTY. I would not have thought so.

Ms. Birrane, I want to stay with you for a little bit longer. As you know, in May, the National Association of Insurance Commissioners sent a letter to Chairman Brown, responding to several questions that he had posed on the topic of alternative asset management companies and the life insurance sector. In NAIC's response, they laid out pretty clearly that State regulators, quote, possess the tools and resources necessary to address Chairman Brown's concerns.

I want to reiterate my support for the role of States as the primary regulators of the insurance industry. And like any other industry, life insurance will continue to evolve, and over the long run I am certain they will provide new and better products as they evolve, to consumers. And, it is clear from NAIC's letter that State regulators have the tools they need to continue in this role. Would you agree with that?

Ms. BIRRANE. Yes, I would agree with that.

Senator HAGERTY. Thank you very much. I appreciate it.

Thank you, Mr. Chairman.

Chairman BROWN. Thank you, Senator Hagerty.

Senator Warren of Massachusetts is recognized.

Senator WARREN. Thank you, Mr. Chairman.

So, not content with buying up hospitals and newspapers and single-family homes, retail chains, and pretty much everything else under the sun, private equity has now set its sights on a new monemymaker, Americans' retirement savings. Over the past decade, private equity has hoovered up companies that sell life insurance and other retirement products, and today, private equity firms control more than 10 percent of all life and annuity assets in the United States despite having had almost zero presence just over a decade ago.

Now these new private equity-owned insurers have developed a particular taste for workers' pensions. Under this model, called the pension-risk transfer, or PRT transaction, private equity giants like

Apollo are buying up pension obligations from big employers like JCPenney and Lockheed Martin and Alcoa. At least 300,000 Americans today have pensions that are managed by private equity firms.

Mr. Seitz, you run the office inside the Treasury Department that oversees insurance products, so I want to ask you about the safety of these Americans' pensions. So let us say someone retired from a company like JCPenney or Alcoa and their pension was transferred over to Athene, Apollo's insurance arm. Would you say that the retirees' pension is just as financially secure now that it is managed by a private equity owner-insurer as it was before?

Mr. SEITZ. No. Thank you, Senator, for that question. I mean, we share your view on the importance of this issue and recognize the importance of pensions to millions of Americans that are relying upon those for their retirement and a dignified retirement, and we are working closely with the NAIC and their regulatory considerations as they look at their framework and how to best address not only changes in the PE sector but also, as Commissioner Birrane mentioned, more broadly in the life insurance sector with regard to their investment and liquidity.

Senator WARREN. Well, I appreciate that you care about these issues, but that is not the question I asked you. I asked you, once there has been a transfer to Apollo's insurance arm, are the people who are covered just as secure as they were before the transfer? That is easy. Yes or no?

Mr. SEITZ. The individuals, when their policies are transferred, as Commissioner Birrane mentioned, they are covered by the individual State guaranty funds. And it is an area of focus for our office to make sure that the State system is being—regulatory mechanisms are being designed appropriately to reflect these new transactions, and we appreciate—

Senator WARREN. I am still not hearing a “yes” or “no.” You know, just to make clear, in a September 2021 report, the Federal Insurance Office, which you run, stated that “PE owners may use investment strategies for their owned insurance entities that have heightened credit and liquidity risk profiles as compared to other market participants” and “tend to hold a more significant proportion of investments in alternative or nontraditional insurance assets that are associated with illiquidity and complexity premiums.” You still agree with what you said?

Mr. SEITZ. No. Thank you, Senator. We have articulated those same points in our letter to Chairman Brown a few months ago, and it is an issue that we are focused on in our office, and we appreciate the changing investment portfolio of those companies as well as across the broader life insurance sector.

Senator WARREN. All right. In other words, there is more risk.

Mr. SEITZ. It is an area of increased focus for our office, and we are looking forward—

Senator WARREN. Look, exposing Americans' retirement savings to more risk is exactly how private equity makes its money. Riskier and more complex investments mean that private equity-backed insurers can jack up their returns and their short-term profits, but the pensions are more vulnerable to being wiped out by a market

downturn which endangers the insurance company's insolvency. This is not hard. This is just how the pieces work.

For example, one-fifth of Athene's portfolio is invested in risky asset-backed securities and leveraged loans made to companies that are already highly in debt, and even worse, many of Athene's risky investments are created or managed by the parent company, Apollo, itself. This means that Apollo collects fees on the investments that it directed its insurance arm to make.

So, look, this is a problem of more risk and the risk is borne by people who have invested for all their working lives in their retirement security, and I want to underline the word "security." My Stop Wall Street Looting Act would strengthen private equity disclosures to empower investors and help regulators crack down on self-dealing, but we also need Federal and State insurance regulators to step up and address the risks that private equity poses to pensioners and workers.

I appreciate that Treasury and NAIC are looking at this issue closely, but enough studying. It is time to act, and I am looking forward to working with both of your offices to ensure that happens.

Thank you, Mr. Chairman.

Chairman BROWN. Thank you, Senator Warren.

Senator Moran from Kansas.

Senator MORAN. Chairman, thank you. Chairman from Ohio, thank you.

Let me start with you, Director Seitz. Concern has been expressed by you and some of my colleagues about private equity firms, however that term is defined, having a short-time horizon for their investments in insurers and thus may be willing to engage in riskier activities. Can you tell me if there are insurers that have been purchased by private equity that have been sold or up for sale, indicating a quick turnaround?

Mr. SEITZ. No. Thank you, Senator. It is an issue that we are closely monitoring, particularly over the last—I think as Commissioner Birrane mentioned, we have seen an increase in activity over the last several years in this area and particularly for certain blocks of business, and it is an area that we are continuing to monitor.

Senator MORAN. The question, though, was: Are there examples of where insurance companies purchased by private equity are then, in a short fashion, sold?

Mr. SEITZ. No. I mean, I do not want to speak to any specific transactions, but I think generally what we have seen is they are not, you know, making those types of movements that you described.

Senator MORAN. Thank you. I do want to indicate that my experience in Kansas is a PE firm's purchase of insurance companies has turned out to be very valuable to that company, to those companies, and it benefited the company and its employees with an influx of capital that fueled growth and additional jobs and helped those insurance companies continue to be in existence and to grow their book of business and their economic activity in our State.

And then I was listening on the television about, and from my office about, a question that the Ranking Member asked. It does seem to me this Administration is determined to import financial

regulations and capital standards from Europe as quickly or as pervasive as they can. My view is that we need the—that we do not need the importation of European policy dictating American business and markets and that the FIO's top priority should be defending American interests and preserving a system that has worked so well, as I heard you indicate, of State regulation over a century in those. You ought to be promoting that in the international forums. And I was not quite certain that you answered Senator Toomey's question, but I would add my thoughts to that topic.

Thank you.

Chairman BROWN. Thank you, Senator Moran.

Senator Sinema is recognized, I believe from her office, Senator Sinema of Arizona.

Senator SINEMA. Thank you, Chairman. I appreciate this.

You know I want to start by talking to our witnesses about our working group that I convened last year, a bipartisan Senate working group with other Members of this Committee to identify and advance solutions around risk sharing and future pandemics. Our goal is to improve the resiliency of the U.S. economy to future pandemic-related economic shocks. Our group aims to do this by creating and advancing an insurance framework that brings forward the power of the private sector and provides business owners with choices to buy coverage that aligns with their needs and their risk tolerance. That will reduce the price tag of any future pandemic response and address some of the waste, fraud, and abuse that we are seeing with respect to pandemic aid.

Our response to future pandemics needs to be leaner, faster, and smarter, and it is important to me that future responses are more fiscally responsible as it is clear that the risk of overspending, coupled with supply chain disruptions, can trigger an inflationary response.

So first, to Commissioner Birrane, I appreciate your joining us today. As you know, for insurance policies that cover event cancellation and business interruption, virtually all of them include an exclusion that exempts pandemics from coverage. Despite this inclusion, I have heard from businesses and insurance brokers alike that event cancellation and business interruption coverage is increasingly difficult to find and it is expensive if you can find it. What do you see in the market for these lines of insurance?

Ms. BIRRANE. Well, I think your characterization of the current market condition is correct, and I do not see that changing in the near future. I think that there are certain types of risk that are, as I have said before, too large, too volatile, too certain for the market to be able to absorb them.

Senator SINEMA. Thank you. Our working group is concerned about this because we want businesses to be able to find and afford the insurance policies they need to qualify for financing and to responsibly plan for the future.

So my next question is also for you, Commissioner. For a future pandemic, I would like to also see an insurance solution for small businesses so that they can take a level of responsibility that aligns with their risk tolerance. In 2020, some Arizona businesses had to wait months to get their PPP loans, and they had to go from bank to bank to access relief. I would rather have a framework where

businesses could purchase subsidized coverage, where it is affordable to the business owner, and the business owner knows exactly how much coverage they are getting. Would you agree that a pre-established, private insurance policy would generally provide faster and more predictable relief for businesses to plan around?

Ms. BIRRANE. Well, what I would suggest is that, you know, the NAIC has supported the idea of a Federal backstop of sorts with respect to BI coverage, and certainly it is important that business owners have a sense of certainty about, you know, what their coverage options are and what their costs are. There are a variety of models that work well when the Government and private industry couple together. That draws on the strength of each, the strength of Government to be able to fund more broadly and the strengths of insurance companies to be able to appropriately underwrite and price and adjudicate claims and assist businesses in risk mitigation.

So I would say, overall, there is a case here to be made for such a partnership and the particular model of that partnership is something that the NAIC does not really have a position on.

Senator SINEMA. Thank you. And would you agree that the risk management and auditing capacities that private insurance brings would be helpful in reducing waste, fraud, and abuse in a future pandemic?

Ms. BIRRANE. I would certainly say that insurance companies, part of what they bring to the table in any circumstance is expertise in underwriting and in risk mitigation as well as risk financing and fraud detection.

Senator SINEMA. Thank you. Now I have a question for you about insurance more generally. In your experience regulating insurance companies, would you say that an insurance carrier bearing some level of risk incentives incentivizes them to conduct more robust auditing and risk management since their own capital is on the line?

Ms. BIRRANE. I would say that insurance companies are very, generally very, effective at reviewing risks and in helping their insureds to mitigate those risks. So that is certainly part of what you get when you have an insurance policy, particularly in the property and casualty area that—or workers' compensation—the insurance company often plays a very integral role through the underwriting process and the pricing process in helping companies to mitigate the risk that they are trying to finance.

Senator SINEMA. Thank you. And finally, I will just say, we are working to identify a thoughtful and bipartisan Federal solution to address this issue and create a smarter response for future pandemics. Our working group appreciates the National Association of Insurance Commissioners strong leadership in endorsing a Federal solution in this space, and I am looking forward to working with you and other key stakeholders to find a path forward here.

So thank you, Mr. Chairman. I yield back.

Chairman BROWN. Thank you, Senator Sinema.

Senator Van Hollen of Maryland is recognized.

Senator VAN HOLLEN. Thank you, Mr. Chairman. Thank you to both of our witnesses here today.

And, Commissioner Birrane, it is great to have a fellow Marylander here. Thank you for your work protecting the interest of Marylanders and your work at NAIC.

And I also want to thank you and NAIC for helping me and some of my colleagues prepare legislation to protect seniors from financial fraud. The legislation is entitled Empowering States to Protect Seniors from Bad Actors Act, and it would provide an authorization grant program to the SEC to provide both State securities and insurance regulators with additional resources to crack down on fraud, which we know is a huge problem, \$3 billion a year at least in financial scams. Can you just speak briefly to the importance of passing this legislation to protect seniors from financial fraud?

Ms. BIRRANE. Absolutely, Senator. We have been very happy to work with you on that initiative. I mean, consumer protection is what insurance regulation is all about, and there is probably no more important area of consumer protection than assuring that our seniors are not subject to aggressive marketing tactics and to, you know, other fraudulent practices. So it is really critically important that we have all the resources available to assure that we are on the ground, working with seniors directly, to be able to prevent them from being caught up in fraud.

Senator VAN HOLLEN. Thank you. And I am going to take this chance to ask the Chairman and the Ranking Member to join us in getting that bipartisan out of the Committee.

Chairman BROWN. Senator Van Hollen, we were just speaking about it quietly while you are asking—

Senator VAN HOLLEN. Thank you. I appreciate that. I thank you. Thank you.

Chairman BROWN. Thank you.

Senator VAN HOLLEN. Let me ask you a couple questions regarding capital standards in the context of climate risk. As you well know, an important role of a State insurance regulator is to monitor the capital adequacy of insurers to ensure their ability to pay their claims following catastrophic events. One of the concerns is that with increasing severity and frequency of extreme weather events that the risk-based capital models may overemphasize the trends of older historical data and not adequately assess newer risk.

So, a two-part question, Commissioner Birrane: What is the NAIC doing to ensure that its models incorporate the most recent and relevant climate data in order to reflect the true risks, and second, from a risk management and capital adequacy perspective, how important is it for insurance regulators to have standardized, comparable data on climate risk?

Ms. BIRRANE. So with respect to the first issue, I would say that what our solvency workstream is doing and what our E Committee is doing is working very closely and making sure that our models are accurate and are up to date, and we are adding additional perils to the RBC capital framework to assure that we capture more broadly the various events that can occur. So that is the first thing.

And second, with respect to data collection, the NAIC has a rigorous process of data collection that we think captures what needs to be captured, and that is something that is subject to constant update and improvement. So we have both on the individual State

level and in the aggregate through the NAIC the ability to capture data in a way that insurance regulators use that data to understand what are claims patterns and where claims are occurring, and why and how, you know, claims are being paid and what the impact of that is on the solvency and the financial status of entities.

Senator VAN HOLLEN. So is there an effort to create some kind of national standard so that States are not using, you know, 50 different standards for this purpose?

Ms. BIRRANE. There is conversation through our center of excellence on the development of a single standard and being able to work through, with insurance companies, what would be appropriate in that regard. So that is a conversation that is occurring as to whether a centralized and standardized approach is the one that makes the best sense, but I want to assure you that in the interim the data collection that occurs around natural disasters and in terms of insurance companies is very robust.

Senator VAN HOLLEN. Thank you.

Mr. Seitz, I do not know if you want to, in my remaining time, just comment on those two parts of that question.

Mr. SEITZ. No. I would just say we share your view on the importance of consistent, comparable, and granular data. I think, particularly for our office, we are looking at it through the lens of the availability and affordability of coverage, particularly in the homeowners' business line, and it is an area that we have seen a need for some national standards and approaches to.

Senator VAN HOLLEN. Thank you. If you could just get for me—I was—we have obviously seen a huge increase in losses, property losses, due to extreme weather events over the last couple decades. There have been a number of reports. If you could maybe try to quantify for me and the Committee what the increased premiums have been as a result of increased climate risk, I realize that is an imperfect science, but I would like a ballpark estimate if you could get back to us on that. All right? Thank you.

Chairman BROWN. Thank you, Senator Van Hollen.

Senator Cortez Masto from Nevada is recognized from her office.

Senator CORTEZ MASTO. Thank you, Mr. Chairman. Thank you to the two speakers today.

First, let me at the very beginning show support for Menendez's, Senator Menendez's, line of questioning around the SAFE Banking Act. The SAFE Banking Act is about supporting small businesses in this country, which are the backbone of our economy, and it is bipartisan, has bipartisan support. I think it should be passed. So I hope my colleagues feel the same way.

Mr. Seitz, Director Seitz, let me talk to you a little about the Federal Home Loan Banks review that is happening. The FHFA recently announced a thorough review of our Nation's Federal Home Loan Banks system. My first question to you is: Are you aware of the proposed review? And if you are, I really have a question about whether the Federal Insurance Office plans to monitor or participate in the review, the Federal Home Loan Banks' review, is going to happen as well.

Let me just put this out there. It was surprising to me to realize that 548 insurance companies are members of the Federal Home

Loan Banks and that they receive about one-quarter of the advances. So I am curious if your organization is going to be reviewing and following what the FHFA is doing.

Mr. SEITZ. No. Thank you, Senator, for that question. The Federal Home Loan Banks play an important role in our housing markets, and we are very well aware in FIO that insurance companies, particularly life insurers, are increasing participants and are taking significant advances from the FHLBs. It is an area that we have been discussing with our colleagues at the FHFA, and we look forward to continuing to engage with them as they begin the review process which just recently started.

Senator CORTEZ MASTO. Good. Thank you. And I hope you do; I hope you do continue to monitor.

Let me jump to an issue that my colleagues have been talking about, which is private equity, but before we get there, I want to follow up on business interruption insurance.

Mr. Seitz, in March of 2020, when the COVID-19 pandemic began, my office received calls from business owners who had bought insurance. They chose policies that included business interruption insurance, and they paid their premiums. Then when the pandemic hit, they had to close down due to a risk of contamination, obviously, but they were not covered.

So I guess my question to both of you is—and you talked a little bit about it. Is it feasible for insurance companies to provide pandemic insurance? That is one.

But then, two, when it comes to private equity, Ms. Birrane, let me ask you this because you talked about in particular the transfer of ownership or risk from private equity to insurance companies. And one of the things you identified is that there are certain types of risk that are too large and too volatile for the market to absorb them, but you do not feel that way about private equity as they come in and purchase so many of, unfortunately, insurance companies and have so much—so many assets.

And I know I am asking and conflating two questions, but they are similarly related. And this is the concern; if insurance companies are not covering the risk when there is a pandemic even though companies are paying for it, if there are some risks related with private equity and there is, God forbid, some disaster economically, how can we guarantee that that coverage will exist by insurance companies as well? Is there a correlation between the two? Do you not see that?

Or, do you feel that protections have been put in place, as you say, Ms. Birrane, by the NAIC adopting these new regulations when it comes to private equity? Maybe let us start with you.

Ms. BIRRANE. Sure. So what I would say is like let us think about this as a matter of contract. So when you think about the business interruption insurance that was baked into policies that were purchased by businesses, those contract terms actually, for the most part, exempted business interruptions that are caused by things like contamination, you know, that would fall within a pandemic or that did not result from a physical covered peril. So from a contract perspective, those gaps in coverage were baked into the policies, and unfortunately, many business owners were not as—were not really aware that those limitations existed.

If we look at private equity as a general matter, I would come back to the notion that the private equity firm, as an owner of the insurance company, does not run the insurance company in the same way. Insurance companies are subject to a set of very clear rules and guidelines around what insurance companies can do, from the kinds of investments that they can make to the credit they get for those investments, to the risk based capital standards that are in place. None of those are different because the owner is a private equity company. So we continue to monitor and regulate the performance of the company regardless of the ownership.

So, hopefully, that helps contrast those two circumstances.

Senator CORTEZ MASTO. And I know my time is running out, and thank you for that. That is very helpful.

But, Director Seitz, do you feel the same way with respect to private equity companies, that they can be adequately protected by additional conditions or these 13 new regulations that NAIC has adopted?

Mr. SEITZ. No. I mean, we appreciate the importance of retirement security products for millions of Americans, and we are working closely with the NAIC and the States as they develop the regulatory considerations. And as our letter noted to Chairman Brown, there are certain areas of focus for our office and also they extend, you know, to the life insurance sector more generally irrespective of sometimes the business models as well.

Senator CORTEZ MASTO. Thank you.

Thank you, Mr. Chairman. I know my time is up. I appreciate it.

Chairman BROWN. Thank you, Senator Cortez Masto.

Thanks, Commissioner, and thanks, Director, both of you, for answering questions forthrightly and being here today and especially for your public service.

I would like to submit for the record the testimony of Colleen Riedel, a retiree of Qwest through the Northwest Bell Telephone Company, a member of Communication Workers of America, whose pension is now administered by Athene.

For Senators who wish to submit questions for the record, those questions are due 1 week from today, Thursday, September 15th.

You would be getting those. To the witnesses, please submit your responses to questions for the record 45 days, no more than 45 days, from the day you receive them. Thank you again.

With that, the hearing is adjourned.

[Whereupon, at 11:26 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

### PREPARED STATEMENT OF CHAIRMAN SHERROD BROWN

Every American needs insurance—whether it’s auto insurance to protect us when we’re on the road, or homeowners’ insurance to protect the biggest investment for most families, or life insurance to cement your family’s financial security in the event of a tragedy.

It’s our job to make sure that the industry is protecting Americans’ hard-earned money—not putting it at risk.

American insurance companies are regulated by State insurance commissioners. The State-based system of insurance regulation is historic, and ensures local markets and needs are taken into consideration.

The National Association of Insurance Commissioners coordinates State commissioners across all jurisdictions, to identify and address risks to the entire system.

In the Wall Street Reform Act, Congress created the Federal Insurance Office within the Treasury Department to promote national coordination in the insurance sector. It’s common sense—insurers operate across all State jurisdictions and internationally.

I’m pleased to have both the Maryland Commissioner Kathleen Birrane on behalf of the NAIC, and Director Seitz of FIO testify today.

If we’re going to keep Americans’ hard-earned money safe, it is more important than ever that they work together.

Today we’ll explore many important topics.

For example, 3 months ago, Lockheed Martin transferred \$4.3 billion of its pensions to Athene Holding—an insurance holding company specializing in life insurance and owned by the private equity firm, Apollo Global Management.

Overnight, Lockheed Martin employees and retirees were notified that their pensions would be managed by Athene and no longer governed by ERISA or the Pension Benefit Guaranty Corporation.

This is just one recent example of private equity giants’ expansion into people’s pensions and the insurance industry.

We know that workers end up worse off when Wall Street private equity firms get involved. We’ve seen it over and over, in industry after industry.

In March, I asked the NAIC and FIO to look into private equity’s expansion into similar pension-risk transfer transactions. We need to understand the risks to workers whose financial security depends on pension and retirement programs.

The NAIC and FIO provided thoughtful responses to my letter. The NAIC has been monitoring the risk-taking behavior of private equity-owned insurers.

FIO has done similar work, and also looked at the wider interconnectedness of insurance and reinsurance markets across the world. Those connections have added to systemic risk concerns, because U.S. insurance companies depend even more on the financial health of insurance companies outside the United States.

Taken together, our insurance authorities are focused on these emerging and complex risks to safeguard our economy.

Our communities and families rely on insurance companies to protect their loved ones, their homes, small business, and so many parts of our lives. We can’t ignore when risks build up, or firms behave irresponsibly.

And we know who always pays the price when they do. It’s not insurance executives. It’s not private equity executives. It’s not Wall Street.

It’s workers and their families. And it’s taxpayers, who were forced to bail out AIG 15 years ago.

That should never happen again.

That also means looking around the corner to make sure the industry and agencies are prepared for risks as they develop. As more Americans face increasingly severe climate catastrophes like wildfires and hurricanes each year, we need to help communities prepare—and we need to ensure insurance watchdogs and the companies they oversee are prepared.

In the aftermath of some of these natural disasters, we have seen instances where insurers either raise prices or stop offering insurance altogether, leaving families and businesses struggling to find affordable coverage as they rebuild their lives and communities.

We also know this industry has a long history of racial discrimination, just like so many big industries.

Black and Brown families face more difficulty in getting insurance across the board. We’ve seen this happen in auto insurance.

Earlier this year, the *New York Times* also reported that customers, insurance agents, and employees sued State Farm for discrimination in the workplace and in paying out claims.

My colleague Chairwoman Waters has been working on learning more about this as well. Her committee recently requested information about large life and P&C insurers' involvement in financing chattel slavery.

And I'm glad FIO and NAIC are also working on this. NAIC is investigating through its Special Committee on Race and Insurance.

And I look forward to reviewing FIO's upcoming report on availability and affordability of auto insurance, and hope it will shed more light on racial equity in accessing this insurance.

Finally, later this year, the International Association of Insurance Supervisors will meet to consider whether the U.S. insurance system's review of capital adequacy standards meets international criteria.

Because we regulate insurance differently here in the U.S., where State and local markets and international markets are served by the same companies, it's important that representatives of the U.S. system like FIO and the NAIC advocate for fair treatment by the international regulators.

And now that the Fed Vice Chair for Supervision has been confirmed, Michael Barr and the offices testifying here today will get to work with our international counterparts in this process.

All of these issues show how critical the work of FIO and NAIC is to our economy's health and stability. I expect FIO and NAIC to prioritize monitoring these risks in their ongoing work.

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#### PREPARED STATEMENT OF SENATOR PATRICK J. TOOMEY

Thank you, Mr. Chairman. And welcome to our witnesses.

It has been quite some time since this Committee has held a hearing on the insurance industry. There are several topics that I'd like to discuss today, including the importance of State-based insurance regulation, efforts to develop international insurance standards, efforts to use the insurance industry to effect changes in social policy, proposals to create a federally guaranteed pandemic risk insurance program, and, finally, the importance of risk-based pricing.

I think it's important to remind everyone that insurance firms are primarily regulated at the State level. Insurers have been chartered and regulated by the States for the past 150 years. When it comes to insurance, the Federal Government has an extremely limited regulatory role, which I see little need to expand.

This system works well for both consumers and industry. That's one reason why we need to pay close attention to efforts to develop and implement international insurance standards by international bodies. In particular, I worry, as do others, that the Insurance Capital Standard, or ICS, currently being developed by the International Association of Insurance Supervisors is incompatible with the U.S. insurance market.

There is widespread concern that the ICS is too sensitive to short-term fluctuations in markets and does not take into account certain assets that insurers hold. As a result, the implementation of ICS in its current form would harm the availability of long-term products that Americans rely on for financial security. Our U.S. representatives at IAIS need to make sure ICS works for the U.S. market by not allowing the proposal to go forward.

Next, I'd like to touch on troubling efforts to use our financial system to address climate change. Some liberal activists want to pressure insurance companies and other financial institutions to deny services to traditional energy companies and other carbon intensive industries. Such efforts are profoundly misguided.

Addressing contentious issues like global warming requires political decisions involving important tradeoffs. We've seen those tradeoffs in action in recent months.

With soaring energy prices, European Nations have made plans to reopen coal power plants and extend the lives of nuclear plants. Likewise, in the U.S. we've seen the Biden administration's hostility to new energy production lead to shockingly high gasoline prices.

That's a painful consequence of their policy choices. In a democratic society, those tradeoffs must be made by elected representatives, who are accountable to the American people, not unelected activists and bureaucrats.

To be sure, insurers face financial risks in the form of natural disasters. After all, that's a core business of the property and casualty insurance industry. Insurers must be allowed to set premiums that accurately reflect such risk, and to the extent climate change exacerbates these risks, they should adjust their prices accordingly.

Higher premiums are an important signal to policyholders that warn of increased risk of fire, flood, earthquake, or other peril. Further, they create a financial incentive to mitigate risk, leading to a safer and more resilient society. The bottom line

is that a well-functioning insurance industry is quite capable of addressing the natural disaster risks it faces today and in the future.

I'd also like to address calls to create a federally guaranteed pandemic risk insurance program. As proposed, this program would be akin to the Terrorism Risk Insurance Program, or TRIA.

As a reminder, TRIA mandates that insurers offer terrorism insurance, and in the event of an attack, the Federal Government bears an increasing share of the cost of claims, depending on the severity. A similar program for pandemics would be misguided.

First of all, it's hard to imagine that insurers are well equipped to quickly distribute hundreds of billions or even trillions of Federal dollars. Recall that in a matter of months the Paycheck Protection Program distributed over half-a-trillion dollars via the banking system, but banks and other financial institutions participated on a voluntary basis. Compare that to the disastrous claims processing after Super Storm Sandy.

But most importantly, a federally guaranteed pandemic risk insurance program would encourage State and local government officials to impose economically devastating shutdowns in the future. Such a program would, in fact, incentivize State and local policymakers to quickly impose lockdowns with the justification that the Federal pandemic risk insurance will bail them out.

Instead of considering policies that will facilitate future lockdowns that repeat the mistakes of the past, we should be thinking about future mitigation measures that don't crush businesses, workers, and the economy, and harm our children's educations.

Let me conclude with this observation. I believe a well-functioning insurance industry is a critical component of economic prosperity and financial security for all Americans. Everyone will be better off if we resist activist efforts to use insurance as a tool to pursue a social policy agenda.

Insurance is not a legitimate tool, as some have suggested, to decarbonize the economy, infringe on the Second Amendment rights of law-abiding Americans, or mitigate wealth inequality.

Let's have insurers stick to the business of insurance. I look forward to discussing these issues today.

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### PREPARED STATEMENT OF KATHLEEN A. BIRrane

MARYLAND INSURANCE COMMISSIONER, ON BEHALF OF THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

SEPTEMBER 8, 2022

#### Introductory Remarks

Chairman Brown, Ranking Member Toomey, and Members of the Committee, thank you for the invitation to testify today. My name is Kathleen Birrane and I serve as the Maryland Insurance Commissioner. As such, I am a member of the National Association of Insurance Commissioners (NAIC), where I serve on the Executive Committee and as the Chair of the Innovation, Cybersecurity, and Technology Committee, Vice-Chair of the Climate and Resiliency Task Force and Co-Chair of the Health Insurance Work Stream of the Special Committee on Race and Insurance. On behalf of my department, my fellow State and territory insurance regulators, and the NAIC, I appreciate the opportunity to testify today. I look forward to discussing the ongoing work of insurance regulators and the NAIC, as well as our views on several topics of interest to this Committee and insurance sector stakeholders.

The U.S. insurance market is the single largest and most competitive in the world. State insurance regulators supervise more than one-third of global premium. As of 2021, the life insurance industry reported \$1.1 trillion in total direct written premium and deposits.<sup>1</sup> Property and casualty insurance companies reported \$798 billion in direct premiums written for 2021.<sup>2</sup> The U.S. insurance industry's cash and invested assets surpassed \$8 trillion at the year-end of 2021.<sup>3</sup> Taken individually, U.S. States make up more than half of the 50 largest insurance markets.

<sup>1</sup> <https://content.naic.org/sites/default/files/inline-files/2021%20Life%20Annual%20Industry%20Commentary.pdf>

<sup>2</sup> <https://content.naic.org/sites/default/files/inline-files/2021-Annual-Property-26-Casualty-and-Title-Insurance-Industry-Report.pdf>

<sup>3</sup> <https://content.naic.org/capital-markets-bureau>

State regulators share a mission to ensure a stable, competitive, and well-regulated insurance marketplace where U.S. consumers are well-informed and well-protected. States work hard to strike an appropriate balance between solvency and product availability and affordability, providing the risk financing that allows individuals and businesses to thrive, while preserving the ability of the sector to meet those financing obligations and pay claims. As we look ahead, we are addressing a number of evolving dynamics, such as the impact of inflation on pricing and claims, the rise of interest rates and the fall of investment returns, risk-taking in insurers' investments, the intersection of race and insurance, climate risk and resilience, cyber risk, and the impact of technology on consumers, companies, and supervisors, among a host of others.

As a national system of State-based regulation, we collaborate closely on a regular basis and have long been committed to providing leadership across the entire spectrum of global and domestic insurance issues and activities. The financial strength of our insurance system was tested simultaneously by a global pandemic, historic natural catastrophes, financial volatility, and social unrest, and yet it persevered. In fact, an S&P Global rating report on the insurance industry found that North America appeared to be the "most resilient region" in the face of COVID-19.<sup>4</sup> That is because as our insurance markets grow and become ever more complex and sophisticated, our regulatory tools and priorities continually evolve. With that, allow me to update you on some of the long-standing and new initiatives State regulators are working on through the open and transparent NAIC process.

### **Innovation, Cybersecurity, and Technology**

State insurance regulators understand that insurers are increasingly using technology, big data, and predictive analytics to reshape the insurance marketplace and the way insurers approach risk and engage with consumers. These technological developments have the potential to improve how an insurer does business and can benefit policyholders. However, we recognize the complexity of these processes and the need to ensure they comply with State insurance laws and regulations designed to protect consumers. Insurance regulators are committed to striking the appropriate balance between encouraging innovation while maintaining the strong consumer protections embedded in our regulatory system.

To this end, last year, we formed a new NAIC Innovation, Cybersecurity, and Technology (H) Committee, which I chair, to address the insurance implications of emerging technologies, cybersecurity, and data privacy. The new committee, and its work, demonstrates our commitment to recognizing the significant impact data and technology is having in the insurance industry and ensures consistent and collaborative coordination among State regulators.

One of the H Committee's key projects is the establishment of a Collaboration Forum as a mechanism for multiple NAIC committees to coordinate their work on issues relating to technology, cybersecurity, and data privacy. The Collaboration Forum bring work groups together to identify and address foundational regulatory issues and to develop a common regulatory framework that can inform further work. The first project of the Collaboration Forum is on algorithmic bias, more specifically, how digital decisional systems and complex predictive models driven by artificial intelligence and machine learning can result in unfair and illegal discrimination in the insurance market. From such inclusive forums we are better able to make informed decisions on how to structure an appropriate regulatory framework around these emerging areas. For example, in the case of insurers' use of AI and algorithmic models for rating, underwriting and other decisional purposes, we are building on the AI Principles that the NAIC adopted two years ago to establish principles-driven guidelines and directives for the application of antidiscrimination laws to the use of artificial intelligence.

Additionally, the committee has several specialized working groups, including a Cybersecurity Working Group, coordinating and communicating amongst State regulators on cyber events, trends, and overall industry cybersecurity posture. It is also developing tools to support State insurance departments' cybersecurity oversight and response duties. Our Privacy Protections Working Group is drafting updates to certain NAIC privacy models, which address insurance privacy protections on the collection, use, and disclosure of information gathered in connection with insurance transactions. Finally, our Big Data and Artificial Intelligence Working Group is analyzing data received through the NAIC's artificial intelligence and machine learning

<sup>4</sup>Dennis P. Sugrue, "Down But Not Out: Insurers' Capital Buffers Are Proving Resilient in the Face of COVID-19", S&P Global Ratings, Sept. 22, 2020, at 9, available at <https://www.spglobal.com/ratings/en/research/articles/200922-down-but-not-out-insurers-capital-buffers-are-proving-resilient-in-the-face-of-covid-19-11656633>.

private passenger automobile survey and initiating similar surveys for homeowners and life insurance. In each of these areas, our work is focused on gaining a granular understanding of how AI/ML supported models are being used by insurers and their vendors across the insurance value chain and, most particularly, in making decisions that impact consumers. These surveys enable State regulators to identify and dig deeply into areas of regulatory concern, such as oversight of third-party data and model vendors and their work product.

State insurance regulators continue to upgrade safeguards to protect the security of data through standards, the examination processes, and model laws. For example, in 2017, the NAIC adopted the Insurance Data Security Model Law, which updated State insurance regulatory requirements relating to data security, the investigation of a cyber event, and the notification to State insurance commissioners of cybersecurity events at regulated entities. Thus far, 21 States (including the State of Maryland) have adopted the model, which covers nearly 3,000 insurers representing over 80 percent of the market by gross written premium. Further, the NAIC is continuing to update and strengthen guidance in its Financial Condition Examiners Handbook to draw more focus to cybersecurity during a financial exam. The NAIC continues to sponsor tabletop exercises with insurers, regulators, and law enforcement to explore cyber incident response and recovery. Maryland will host its tabletop exercise this October. Finally, we engage with State and Federal counterparts on cyber security issues impacting our Nation's financial infrastructure, through the Financial and Banking Information Infrastructure Committee (FBIIC).

### **Race and Insurance**

Another area of significant activity for State insurance regulators is the intersection of race and insurance. In 2020, in the wake of a national call to action on race and inequality issues, the NAIC created a Special Committee on Race and Insurance, the first of its kind in NAIC history, to evaluate racial inequity in the insurance sector. Our formation of such a committee was emulated by others throughout the insurance sector leading to a national discussion on this important topic. The committee is focused on addressing access to the insurance sector and market barriers to the acquisition and use of insurance products by researching: (1) the level of diversity and inclusion within the insurance sector and developing recommended action steps for insurance regulators and companies that reflect a broad consensus among NAIC members; (2) diversity, equity, and inclusion best practices within State insurance departments and developing forums for sharing relevant information among States and stakeholders; and (3) barriers that may disproportionately impact people of color and/or historically underrepresented groups within the property and casualty, life insurance and annuities, and health insurance lines of business.

This year we have taken a particular focus on addressing barriers that prevent or limit access to the insurance market. As we identify these barriers, we are formulating targeted strategies that open up the insurance market to diverse and underserved communities. We firmly believe that if more consumers have the benefit of protections provided by quality products they and their families will be better protected and, in a position, to build generational wealth.

We are also pleased to share that the NAIC has formed the New Avenues to Insurance Careers Foundation. The Foundation will focus on fostering interest in careers in insurance and insurance regulation, with particular focus on students from underserved and diverse communities. We believe the lack of diversity in the insurance sector is one of those barriers to entry that we can help address. As a result, this is an important step that will advance one of the key goals of the Special Committee on Race and Insurance and support our members' efforts to increase diversity and inclusion in the regulatory community.

State regulators believe there should be equal access to insurance markets and products, and we must ensure that insurance companies are not unfairly discriminating at any stage of the insurance process, from underwriting to rate setting, to claims handling. The volume of data being created, combined with ever evolving computational techniques, have resulted in unprecedented data mining capabilities that fuel the development of predictive models used to support decision making by insurers. These AI/ML driven decisional systems can and do incorporate and amplify unfair bias which can result in unfair discrimination when applied to consumers. The Algorithmic Bias Project of the H Committee's Collaboration Forum is addressing unfair algorithmic bias, how it emerges, and the right regulatory approach to mitigation and detection. The Project recently held a multiday collaboration session for State insurance regulators featuring academics and experts on this topic. These issues are complex and far reaching, and our work is necessarily measured and de-

liberative to avoid unintended consequences in the market. We are committed to continuing these important efforts and welcome your engagement.

### **Climate Risk, Natural Catastrophes, and Resiliency**

Another top priority for the NAIC is climate risk and resiliency. State insurance regulators, through the NAIC, have had a climate-specific working group for more than a decade. In 2020, the working group evolved into our Climate and Resiliency Task Force, which serves as the coordinating NAIC body for discussion and engagement on climate-related risk and resiliency issues. It builds on existing efforts to address the economic consequences of natural disasters, including efforts to mitigate their toll. In addressing this evolving risk, we are focusing on the analysis of climate-related financial risk, the availability and affordability of insurance, and stakeholder risk awareness and engagement. We continue to advocate for resiliency and mitigation efforts that can reduce the risk of property loss. This keeps people in their homes and businesses open. Resiliency and mitigation are particularly important for communities that cannot afford to bear the burden of catastrophes and are most challenged to recover.

Our detailed work to address climate-related risks in the insurance sector is highlighted in our letter to the U.S. Department of the Treasury regarding its request for information for its upcoming climate report.<sup>5</sup> The NAIC also issued a report titled, “Adaptable to Emerging Risks: The State-Based Insurance Regulatory System is Focused on Climate-Related Risk and Resiliency.”<sup>6</sup>

Of note, this year, our Task Force facilitated revisions to the Climate Risk Disclosure Survey for participating States, which is now aligned to the Financial Stability Board’s Taskforce on Climate-related Financial Disclosure (TCFD). The survey, which was first adopted by the NAIC in 2010, is a risk management disclosure tool for States to require of their insurers. These disclosures help insurance regulators assess and evaluate insurance industry risks and actions to mitigate climate risk. Currently, 15 States are participating in the survey with nearly 80 percent of the market captured by direct written premium. This year, participating States will require licensed insurers writing at least \$100 million in direct premium to publicly report a TCFD.

State insurance regulators also continuously monitor the capital adequacy of insurers to ensure their ability to pay claims following catastrophic events. A fundamental tool for monitoring capital adequacy is the NAIC’s Risk Based Capital (RBC) formula, which determines the minimum amount of capital an insurer should hold based on its risk profile. Regulators continually update RBC charges to address the evolving risk landscape. For example, in 2017, the NAIC expanded the risks quantified in the RBC formula to include a specific charge for hurricane and earthquake catastrophe risk in order to recognize increased exposure to catastrophic events. Most recently, the solvency workstream of the Task Force recommended that wildfires be added to the RBC framework for catastrophe risk exposures. In addition, based on the recommendations of the Task Force, the NAIC’s Financial Condition Committee is considering specific enhancements to the solvency oversight tools used by State insurance regulators that will expand the evaluation of an insurer’s exposure and response to climate-related financial risk, particularly in areas such as transition risk. The Task Force is also evaluating viable approaches to scenario analysis and stress testing for insurers as the data necessary to conduct such exercises becomes available.

The role that State regulators play with respect to climate risk involves more than just ensuring financially strong insurance companies and a viable market; it also includes ensuring strong and resilient homes and communities. Insurers are risk financers and, as such, are risk managers and risk mitigators. Leveraging that, our members are leaders in the effort to help State and local governments build more resilient communities. State insurance regulators encourage the use of innovative building materials, technology, and mitigation methods to reduce the impact of climate risk across a broad spectrum of natural catastrophe risks, and, most importantly, they work with insurers to design new and innovative products, and to establish partnerships with insurers that can help guide and finance community efforts.

Significantly, the NAIC has established a catastrophe model center of excellence within its Center for Insurance Policy and Research. This center will provide State insurance regulators with access to information, education, and training regarding

<sup>5</sup> <https://content.naic.org/sites/default/files/testimony-letter-response-fio-rfi-climate-financial-risk-211111.pdf>

<sup>6</sup> <https://content.naic.org/sites/default/files/climate-resiliency-resource-report-adaptable-emerging-climate-related-risk-resiliency-2021.pdf>

catastrophe models, as well as conduct applied research to address regulatory climate risk and resilience priorities.

### **Financial Regulatory Oversight**

Turning to our continued efforts to ensure effective insurer financial solvency regulation, we would like to highlight a few specific developments in addition to those already referenced. Over the past decade, State insurance regulators have made many enhancements to group supervision, informed by lessons from the financial crisis. We have expanded and strengthened our holding company statutes, implemented stronger corporate governance requirements, and now require larger insurers to file an Own Risk and Solvency Assessment (ORSA), which is a globally recognized report of all the risks posed to an insurance group, both from within the insurers, and from non-insurance affiliates regardless of their geographic location. Additionally, we have rolled out our Group Capital Calculation (GCC), giving regulators groupwide insight into capital allocation. Those improvements demonstrated their value over the last 3 years where even in the midst of historic market volatility and stress, the U.S. insurance sector proved to be financially strong and resilient.

### **Group Capital Calculation and Liquidity Stress Test**

The NAIC's Insurance Holding Company System Regulatory Act and Insurance Holding Company System Model Regulation have historically provided State insurance regulators with the framework for insurance group supervision. In 2020, the NAIC adopted revisions to these models to create a GCC and Liquidity Stress Test (LST).

The GCC adds another analytical tool to State insurance regulators' toolbox on group supervision. It assists regulators in holistically understanding the financial condition of non-insurance entities. It provides key financial information on the insurance group, quantifies risk across the insurance group, supports transparency into how capital is allocated, and aids in understanding whether and to what degree insurance companies may be supporting the operations of non-insurance entities. The GCC was built to strengthen State regulation, but it also serves to satisfy the group capital assessment requirements of the Covered Agreements with the EU and U.K.

The LST was developed to provide State insurance regulators with insights into a key macroprudential risk monitored by the Financial Stability Oversight Council (FSOC) and other jurisdictions internationally, but it also enhances group supervision. The LST requires insurers to file the results of a specific year's Liquidity Stress Test with the lead State insurance commissioner.

### **Credit for Reinsurance Model Law**

With regard to reinsurance collateral, in 2017, the U.S. Department of the Treasury and the United States Trade Representative, concluded negotiations on an agreement with the European Union that eliminates U.S. collateral requirements for EU reinsurers provided certain regulatory criteria are met. In 2018, a separate Covered Agreement was signed between the U.S. and the U.K., which mirrors the language from the agreement with the EU and has the same timing requirements for implementation. The EU and U.K. have agreed to recognize the States' approach to group supervision, including group capital, and eliminate any local presence requirements for U.S. firms operating in the EU. The U.S. and EU have 5 years until September 2022 to comply with the Agreement's provisions, and we are confident the States will meet our obligations.

In June 2019, the NAIC adopted revisions to the NAIC Credit for Reinsurance Model Law and Model Regulation that are intended to implement the reinsurance collateral provisions of the Covered Agreements. The revisions eliminate reinsurance collateral requirements for reinsurers that have their head office or are domiciled in any of the following "Reciprocal Jurisdictions": an EU-member country (or any other non-U.S. jurisdiction) that is subject to an in-force covered agreement, thereby addressing the elimination of reinsurance collateral requirements with U.S. ceding insurers; a U.S. jurisdiction that meets the requirements for accreditation under the NAIC financial standards and accreditation program; and a non-U.S. jurisdiction recognized as a Qualified Jurisdiction that meets additional requirements consistent with the terms of a covered agreement. For reinsurers domiciled in Qualified Jurisdictions to obtain similar treatment as those jurisdictions subject to the Covered Agreements, they must provide to the States the same treatment and recognition afforded by EU countries pursuant to the EU/U.S. Covered Agreement. Therefore, our revisions include the requirement that the Qualified Jurisdiction must agree to recognize the States' approach to group supervision, including group capital. As of August 2022, 56 jurisdictions have adopted the 2019 revisions to the Credit for Reinsurance Model Law. With respect to the Credit for Reinsurance

Model Regulation, 52 jurisdictions have adopted so far, and another four are pending (the District of Columbia, Florida, New Jersey, and the U.S. Virgin Islands). These numbers include America Samoa, Guam, and the Northern Mariana Islands who issued orders bringing them into compliance with the Covered Agreements.

### **Private Equity**

Turning to an issue that has generated significant media attention and Congressional interest, State insurance regulators have been actively monitoring the recent growth of alternative asset management companies, private equity (PE) firms among them, in the life insurance sector.

It is important to emphasize that any insurer, regardless of its ownership structure, is subject to a comprehensive regulatory regime that is experienced at both microprudential and macroprudential supervision. These existing regulatory requirements, designed explicitly to protect policyholders, have been refined and strengthened by lessons learned from past recessions, natural disasters, terrorist attacks, the 2008 financial crisis, and most recently the COVID-19 pandemic, all of which put our system to the test. Our system focuses on risks at the individual insurer and group level, with extensive disclosure, analysis, capital requirements, and regulatory authority to protect solvency, while promoting product availability and affordability. The form of ownership is generally irrelevant to the financial oversight and supervision. Where it is considered, it is generally a basis for enhanced supervision and reporting.

The State regulatory approach to PE firm ownership of insurers corresponds to what typically motivates PE investment in insurers and the concerns that arise from those motivations. PE and alternative asset manager interest in the insurance sector is driven by access to a large pool of assets, primarily in the form of mandatory reserves, that are available for investment. A decades long low interest environment has placed pressure on insurers to take more risk in a percentage of their investment portfolios in order to increase yield. PE firms and alternative asset managers believe that they are better equipped to structure investments that will provide that yield and generate better returns that will benefit both the insurer (and, hence, its policyholders) and the PE firm/alternative asset manager. While recognizing that potential, State regulators have also recognized the risks associated with such investments and have been proactive in addressing those risks.

State regulators first came together through the NAIC in 2013 to consider concerns arising from the proposed acquisition of certain insurers by PE firms. In light of what was then a new market dynamic, regulators premised approval of several early transactions on additional stipulations designed to provide greater safeguards in the form of greater regulator optics, oversight, and control with respect to financial transactions, investments, distributions, and reporting. A list of some of these stipulations was published by the NAIC as best practices and, in time, the additional stipulations were included in the NAIC's Financial Analysis Handbook, a process manual that is used by all States in performing their financial analysis of their domestic insurers, including analysis triggered by an acquisition or other significant financial event.

In addition, State regulators are particularly mindful of investment strategies by some PE-controlled insurers that may be more aggressive than traditional insurance asset managers. State insurance regulators continue to review and refine existing guidance to ensure their ability to assess and address the risks to the insurers. It should be noted, however, that some of these affiliated arrangements are not limited to just private equity owned companies. Increasingly, we have seen traditional life insurers also adopt some of these structures.

The NAIC's Macroprudential Working Group has developed a list of 13 regulatory considerations related to their ability to adequately assess risks posed to insurers because of recent increases in the complexity of investments and other developments. This list is being used to identify where existing disclosures, policies and/or procedures should be modified, or new ones created, to address any gaps based on the increase in the number of PE owners of insurers as well as the increase in asset managers' involvement in insurance, the increase of private investments in insurers' portfolios, and other causes. Our work here is focused on the activities in question, and therefore not limited to private equity backed insurers alone. The prolonged low interest rate environment has been challenging for life insurers in particular, who must take on enough risk in their portfolios to generate yield sufficient to pay claims without raising rates too high for consumers, while satisfying regulators' requirements to protect solvency and pay claims. We have extensive data reporting and analytical capability, to review and assess alternative investments or unique structures, and we are continuing to refine those tools as we speak. More

specifics of this work are highlighted in our letter to Chairman Brown regarding his request for information on this issue.<sup>7</sup>

### **S&P Global's Rating Proposal**

Another noteworthy issue we wrote to this Committee about was S&P Global's proposal to revise its methodology for assessing insurers' financial strength, Insurer Risk-Based Capital Adequacy—Methodology and Assumptions.<sup>8</sup> While S&P ultimately withdrew its proposed approach and the NAIC typically refrains from commenting on the methodologies of the Nationally Recognized Statistical Ratings Organizations (NRSROs), this proposal compelled us to raise our concerns.

As background, insurer investments typically fall into one of two categories—investments assigned a rating by a NRSRO recognized by the NAIC, and investments that are not rated by a NRSRO and for which the NAIC's Securities Valuation Office (SVO) then performs a credit risk assessment on behalf of State insurance regulators. Most U.S. insurer investments fall into the first category and are rated by at least one of the NRSROs. Those investments are then assigned an NAIC designation for the purpose of identifying capital requirements associated with the risk. NAIC designations derived from NRSRO ratings are mapped directly to those NRSRO ratings with no additional analysis conducted by SVO staff. Further, because we do not conduct additional analysis, all NRSRO ratings effectively are treated equally by our system.

While this reliance on NRSROs may have benefits in terms of regulatory efficiency, given the extensive nature of the sector's holdings, it has been an area of concern for the NAIC. This concern has grown as discrepancies between various NRSRO ratings for the same security have increased in recent years, introducing greater potential for "rating shopping" by our sector. Indeed, the NAIC's Valuation of Securities Task Force, comprised of regulators from around the country, has put this concern on its agenda for 2022.

As outlined in our letter, we had concerns with a key aspect of the S&P proposal. Specifically, for those investments not otherwise assigned a rating by the NRSROs (e.g., private placements, certain asset backed securities, etc.), the NAIC SVO staff do conduct a detailed analysis to evaluate the risk and develop an appropriate NAIC designation for use by State insurance regulators. This, coupled with investment oversight laws, gives State regulators comfort to allow or disallow such investments and ensure they are backed by sufficient capital for claims payment purposes. This is a critical regulatory function that allows the insurance sector to invest its substantial resources in a diverse cross section of the U.S. economy while prioritizing the strength of insurers to pay claims. We were troubled that S&P's (withdrawn) proposal lumped NAIC designations assigned by the SVO staff, designed by and for regulators, in with NAIC designations derived from ratings provided by S&P and its for-profit competitors, with no input from regulators or SVO staff. This could have disrupted a critical source of diversification and investment for the U.S. insurance sector.

### **International Engagement**

On the international front, State insurance regulators and the NAIC continue to engage with international colleagues on a variety of important issues at the International Association of Insurance Supervisors (IAIS). Over the past few years, the IAIS has been working to finalize and implement key post-financial crisis reforms as well as pivot to better address emerging issues—a number of which I have already touched on: innovation and technology; cyber; diversity, equity, and inclusion; and climate and resiliency. As founding members of the IAIS, the NAIC and its members are pleased to continue sharing our expertise and knowledge, as well as learning from other jurisdictions as we collectively look to address the evolving risks, challenges, and opportunities in the insurance sector.

On financial stability, we contributed to developing the IAIS Holistic Framework for systemic risk in the insurance sector and welcomed its adoption in 2019, as it provides a variety of tools, fosters better understanding of potential risks and incorporates an activities-based approach rather than relying solely on an entities-based approach. As focus on macroprudential supervision has expanded, we have been pleased to share our domestic experiences on topics such as data collection and analysis, liquidity stress testing, and private equity. Jurisdictions around the globe, including the U.S., have made great strides to implement the Holistic Framework and

<sup>7</sup> <https://content.naic.org/sites/default/files/government-affairs-letter-naic-pe-response-sen-brown-220531.pdf>

<sup>8</sup> <https://content.naic.org/sites/default/files/government-affairs-letter-s%26p-proposed-capital-model-house-financial-services-cmte-030922.pdf>

having this better approach for systemic risk in place should convince the Financial Stability Board to discontinue identification of global systemically important insurers when it comes time to make such a decision later this year.

In addition to financial stability, another post-financial crisis key area of focus has been improving groupwide supervision. Another important IAIS milestone in 2019 was adoption of ComFrame, the Common Framework for Supervision of Internationally Active Insurance Groups, or IAIGs. IAIGs are defined as groups with more than \$50 billion in assets or \$10 billion in Gross Written Premium, operating in three or more countries and doing at least 10 percent of their business outside of their home jurisdiction. ComFrame helps foster better cooperation and coordination amongst those involved in supervising IAIGs. Since its adoption, work has been underway to review ComFrame and identify ways to incorporate it into our own regime in an appropriate manner, including revisions to our financial analysis and examiners handbooks.

One part of ComFrame yet to be finalized is the Insurance Capital Standard (ICS). Additionally, the U.S., with input from other interested jurisdictions, is developing the Aggregation Method (AM) as a comparable alternative to the ICS. Both the ICS and AM are intended to be applied to IAIGs.

The ICS is in the third year of a 5-year monitoring period, the purpose of which is to monitor the performance of the ICS over time and inform any potential improvements before finalizing and adopting. Another key decision to be made at the end of the monitoring period is whether the AM provides comparable outcomes to the ICS. If deemed comparable, the AM will be considered “outcome-equivalent” to the ICS. This summer, the IAIS conducted a public consultation on detailed draft criteria that will be used to assess comparability. Such consultations provide transparency, which is something we push for at the IAIS, as well as an opportunity to hear directly stakeholders’ views and receive their feedback, which should help shape revised criteria. IAIS members agreed that the comparability assessment should neither give the AM a free pass nor preclude comparability at the outset. Keeping this in mind will be crucial as the IAIS works to finalize the criteria later this year and to ensure a fair path forward for the AM by focusing on the outcomes produced by these two approaches rather than their conceptual differences.

The NAIC, as well as the U.S. Department of the Treasury and the Federal Reserve, have been clear with the IAIS, and international colleagues, that the ICS does not work for the United States market or our supervisory regime, and therefore States will be implementing an AM approach. The AM leverages proven legal entity reported available and required capital to produce a measure of group capital adequacy. For the State system, the AM is implemented as the Group Capital Calculation referenced previously, and for the Federal Reserve, it is the Building Block Approach. These complementary approaches provide a group lens on solvency while maintaining legal entity building blocks that allow supervisors to analyze, identify, and address capital deficiencies where they reside.

We, and hopefully the rest of Team USA, will continue to advocate for recognition of the U.S. approach to group capital. Absent recognition through either a comparability process or some other means, the IAIS will have failed in its goal of a global approach to evaluating group capital.

While we hope for the best outcome on comparability, as you have heard, this is just one of many projects, topics, and priorities at the IAIS, and we will continue to remain at the table and work together with our international colleagues on this broad array of issues in order to protect policyholders and contribute to financial stability.

### **Federal Policy Priorities**

Finally, while State insurance regulators are putting significant energy into our regulatory priorities this year, we also would like to highlight several Federal priorities.

First, we urge Congress to pass a long-term reauthorization of the National Flood Insurance Program (NFIP) prior to its September 30, 2022, expiration to provide certainty for insurance consumers. The NAIC’s guiding principles<sup>9</sup> for NFIP Reauthorization for Congress emphasize the importance of long-term reauthorization, encourage greater private market growth to help provide consumers with additional choices for flood insurance products, and increase investment in mitigation planning. Insurance regulators support the inclusion of mitigation discounts—such as premium discounts or insurance rate reductions to persons who build, rebuild, or retrofit their properties to better resist flood events—and allowing individuals to set

<sup>9</sup> <https://content.naic.org/sites/default/files/inline-files/government-relations-161019-nfip-guiding-principles-0.pdf>

aside funds in a tax-preferred savings account for disaster mitigation and recovery expenses. We also support the Disaster Mitigation and Tax Parity Act (S. 2432) that would ensure that State-based disaster mitigation grants receive the same Federal tax exemptions as Federal mitigation grants. This would help provide greater incentives for homeowners to protect their homes from natural disasters. These actions, along with building and maintaining structures that incorporate mitigation strategies, have the potential to reduce future program losses and improve the financial condition of the NFIP.

Second, the NAIC and State regulators would like to thank Senator Tim Scott for introducing the Primary Regulators of Insurance Vote Act of 2022 (S. 4110), which would provide State insurance regulators with a vote on the Financial Stability Oversight Council (FSOC). Currently, State regulators have a nonvoting seat on FSOC. The insurance sector—which historically has been a primary focus of FSOC—is the only financial services sector whose primary regulator is not a voting member. We encourage Members of this Committee to support the Primary Regulators of Insurance Vote Act.

Finally, the NAIC is working on proposed legislation that would help protect policyholders during insurance receivership proceedings. Current law provides no deadline to the Federal Government for filing claims in an insurance receivership. This causes the proceedings to drag on for years and reduces recoveries for consumers. The NAIC is working on proposed legislation that would set a deadline for the Federal Government to file claims it may have against insolvent insurance companies. We encourage Members of this Committee to cosponsor and support the legislation once it is introduced.

### **Conclusion**

As you can see, there is considerable activity by State insurance regulators on a variety of important topics in a variety of venues. The NAIC and State regulators continue our ongoing efforts to improve regulation in the best interests of U.S. insurance consumers while fostering an innovative and competitive insurance sector. State regulation has a strong 151-year track record of evolving to meet the challenges posed by dynamic markets, and we continue to believe that well-regulated markets make for well-protected policyholders. Thank you again for the opportunity to be here on behalf of my fellow Commissioners who make up the NAIC. I look forward to your questions.

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### **PREPARED STATEMENT OF STEVEN SEITZ**

DIRECTOR, FEDERAL INSURANCE OFFICE, U.S. DEPARTMENT OF THE TREASURY

SEPTEMBER 8, 2022

Chairman Brown, Ranking Member Toomey, and Members of the Committee, thank you for the opportunity to testify today about current issues in insurance. I am the Director of the Federal Insurance Office (FIO) within the U.S. Treasury Department.

I would like to begin by briefly outlining FIO's role and responsibilities, and by describing some of FIO's current priorities.

The United States is the world's largest insurance market, and its insurers provide a diverse range of products to support the needs of consumers and businesses in the United States. The U.S. system of insurance regulation is primarily State-based; however, FIO has a significant role to play, as reflected in its statutory duties and authorities. FIO advises the Treasury Secretary on major domestic and prudential international insurance policy issues; coordinates Federal efforts and develops Federal policy on prudential aspects of international insurance matters—including representing the United States at the International Association of Insurance Supervisors (IAIS); assists the Treasury Secretary in administering the Terrorism Risk Insurance Program (TRIP); monitors the extent to which traditionally underserved communities and consumers, minorities, and low- and moderate-income persons have access to affordable insurance products regarding all lines of insurance, except health insurance; assists the Secretary in negotiating covered agreements with foreign jurisdictions; and monitors the insurance industry, including identifying issues or gaps in the regulation of insurers that could contribute to a systemic crisis. As FIO's Director, I also serve as a nonvoting member of the Financial Stability Oversight Council. Finally, FIO regularly and extensively consults with the States, including State regulators, regarding insurance matters of national importance, as well as on prudential insurance matters of international importance. These authorities reflect the need for FIO to provide a national, Federal perspective in this critical area.

Every year, FIO issues a report on the insurance industry.<sup>1</sup> FIO's next annual report will be published later this month. Separately, by the end of this year, FIO will submit its annual joint report with the Federal Reserve Board on our efforts with respect to global insurance regulatory or supervisory forums, as required by the Economic Growth, Regulatory Relief, and Consumer Protection Act.

I would like to highlight five current FIO priorities.

Climate-related financial risk is a top priority for FIO. We are focused on three areas, which are consistent with President Biden's Executive Order on Climate-Related Financial Risk.<sup>2</sup> First, FIO plans to publish a report assessing climate-related issues and gaps in the supervision and regulation of insurers. Second, FIO is evaluating the potential for major disruptions of private insurance coverage in U.S. markets that are particularly vulnerable to climate change. The adverse effects of climate change are disproportionately borne by financially vulnerable communities, which have fewer resources and may face challenges in finding affordable insurance. Third, we are increasing our engagement domestically and internationally on climate-related financial risk issues. As we move forward with these efforts, we will also seek consistent, comparable, and granular data to increase our understanding of the risks from climate change to policyholders, insurers, and the financial system.

A second focus area for FIO is the growing role of alternative asset managers, such as private equity firms, in the U.S. insurance sector. This evolution—which includes but is not limited to increased private equity ownership of U.S. insurers—is one that our office has highlighted for several years. It warrants increased attention to ensure that regulatory mechanisms are appropriately designed to address the activities and market developments highlighted in our recent letter to Chairman Brown.<sup>3</sup> FIO's upcoming annual report will further address this topic, and we encourage continued focus and increased progress by State regulators in this area. FIO will continue to prioritize four areas for research and action on this topic: (1) liquidity risk, (2) credit risk and capital adequacy, (3) offshore reinsurance implications, including increased interconnectedness between the U.S. and Bermuda insurance markets, and (4) potential conflicts of interest.

FIO is also focused on cyber-related risks, which is a top priority for Treasury and the entire Federal Government. FIO has been examining insurers' own cyber resilience, as well as the development of the cyber insurance market and how it may help improve policyholder resilience to cyber events and also serve as a risk-management tool. FIO has increased its data collection in this area with regard to TRIP and has supported the development of Treasury's counter-ransomware strategy.<sup>4</sup> FIO is working with the Department of Homeland Security's Cybersecurity and Infrastructure Security Agency (CISA) in connection with the Government Accountability Office's recommendation that FIO and CISA jointly assess the need for a Federal backstop for cyber insurance. FIO is coordinating closely with the White House Office of the National Cyber Director on these issues. Relatedly, we will be working with CISA as it implements the Cyber Incident Reporting and Critical Infrastructure Act of 2022. Finally, FIO continues to monitor and coordinate with the NAIC and States on cyber-related risks.

A fourth priority for FIO is our representation of the United States at the IAIS, in close coordination with the Federal Reserve, the NAIC, and the States. In addition to its focus on climate, private equity, and cyber, the IAIS is considering other important topics such as the development of the Insurance Capital Standard (ICS) and the related comparability work involving the aggregation method, as well as the implementation of the Holistic Framework for the assessment and mitigation of systemic risk in the insurance sector. The development of the ICS, the aggregation method comparability assessment, and the IAIS's macroprudential work are important global initiatives that will affect the U.S. insurance sector, and it is critical for FIO and the United States to remain engaged at the IAIS on these issues as the international community develops global standards for the insurance sector.

Fifth and finally, FIO is prioritizing work on diversity, equity, and inclusion, or "DE&I." Consistent with FIO's statutory authorities, FIO looks at these issues through the lens of the availability and affordability of insurance products, particularly for traditionally underserved communities and consumers, minorities, and low-

<sup>1</sup> FIO's 2021 Annual Report on the Insurance Industry and other FIO publications are available at <https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/federal-insurance-office/reports-notice>.

<sup>2</sup> Executive Order 14030 (May 20, 2021).

<sup>3</sup> See letter from U.S. Department of the Treasury to The Honorable Sherrod Brown (June 29, 2022), <https://www.banking.senate.gov/imo/media/doc/fio-85.pdf>.

<sup>4</sup> See FIO, Report on the Effectiveness of the Terrorism Risk Insurance Program (2022), <https://home.treasury.gov/system/files/311/2022%20Program%20Effectiveness%20Report%20%28FINAL%29.pdf>.

and moderate-income persons. Right now, FIO is working to update its study on personal auto insurance affordability. Additionally, DE&I issues are also key components of our upcoming climate work.

On all of these topics, and many others, FIO values our close relationship and frequent coordination with State regulators, the NAIC, our Federal partners, and international counterparts, as well as insurance industry stakeholders.

Thank you again for the opportunity to testify today.

**RESPONSES TO WRITTEN QUESTIONS OF CHAIRMAN BROWN  
FROM KATHLEEN A. BIRrane**

**Q.1.** With historic heat waves, wildfires, floods, droughts, and extreme storms this summer, communities across the country found climate disaster knocking at their door. Black and Brown families especially living in disaster-prone areas have borne the brunt of these crises each time. As climate change increases the severity and frequency of storms and disasters, more and more Americans will face risks not only to their lives, but to their homes, cars, and businesses. How do these increasingly severe climate events impact the affordability and availability of insurance to families across the country?

**A.1.** As State insurance regulators, we strive to maintain the critical balance between insurer solvency and reasonable rates, which can be challenging in certain areas that insurers view as presenting a greater risk of loss. As losses continue to rise, insurers must have enough funds to pay claims, making it critically important that we do what we can predisaster to mitigate the potential impacts of catastrophes. Risk reduction and mitigation can protect consumers and reduce the losses paid by insurers—or otherwise absorbed through Federal spending—helping to maintain solvent insurance markets while keeping rates more affordable. Through the NAIC’s Climate and Resiliency Task Force, we have been working with consumer stakeholders to help promote mitigation to individual consumers. Individual resilience is only part of the solution. The most vulnerable communities may benefit more from whole-community protection. Underserved communities are the least likely to have adequate insurance and the least likely to be able to afford mitigation retrofits, which is why resiliency funding is essential. For this reason, the Task Force is also exploring community-based solutions and working with States to identify resiliency funding programs and public–private capital frameworks.

**Q.2.** Insurers help policy holders deal with unexpected risk to their homes, their businesses, or their loved ones. Insurers assume this risk in the hope that premiums will generate profits—or return on capital. When excessive risk is taken, policy holders and the entire economy can be at risk. Reinsurance—the practice of transferring risk to others—can pose a threat to policy holders and annuitants and is seen as a potential blind spot for regulators as some firms have as much as 80 percent of their obligations placed with offshore reinsurers. That can mean hundreds of thousands of workers and families facing increasing risks when insurers hold less capital and there is little or no transparency about where those assets are held. What is the risk to State guaranty systems if U.S.-based insurers use offshore reinsurance to hold less capital, so that in time of crisis, and States must foot the bill to policyholders?

**A.2.** Reinsurance serves a valuable function for both insurers as well as the U.S. economy, because it allows U.S. insurers to write the coverage that U.S. consumers and the U.S. economy needs, but does so by accessing markets beyond the U.S. This assists with both risk mitigation and diversification of U.S. insurers. Historically, offshore reinsurance has been and continues to be used extensively and successfully by U.S. property casualty reinsurers for

these specific reasons. Over the past decade, U.S. life insurers have also begun to utilize offshore reinsurance more extensively. The NAIC believes that what is driving the increase in cessions to offshore reinsurers is the low interest rate environment and potential tax advantages offshore. The increase in cessions to non-U.S. reinsurers has also been caused by an elimination of collateral requirements as a result of the Covered Agreements and resulting change in the States approach to reinsurance credit risk.

State regulators require U.S. insurers to identify each reinsurer they utilize in the annual statutory financial statements, along with key information on each of those cessions (ceded reserves, ceded premium, jurisdiction, credit rating, etc.). This information is used to help understand the credit risk associated with each U.S. insurers reinsurance strategy. The information is also used within each U.S. insurer's annual Risk-Based Capital filing to set aside capital for this credit risk. Prior to the Covered Agreement, State regulators also mitigated credit risk associated with offshore reinsurance with the use of collateral requirements on cessions to reinsurers outside of the U.S. The State-based system of financial oversight of insurers is focused on preventing insolvencies.

Because the U.S. regulator continues to closely monitor the financial performance of the U.S. insurer, regardless of its reinsurance arrangements, the mere ceding of business to an offshore reinsurer does not make it more likely that a U.S. insurer will fail. Each U.S. insurer is required to hold enough capital to compensate for any additional credit risk that might be associated with ceding a large portion of their business to a reinsurer with a lower credit rating. Additionally, as U.S. regulators see insurers with a greater cession to a non-U.S. insurer that may pose a greater amount of credit risk to the insurer, the regulator would request the insurer further diversify their credit risk through additional reinsurers.

Further, in the event that an offshore reinsurer that is not required to post collateral to back-up its reinsurance obligations (under agreements made by the Federal Government) fails to meet its reinsurance obligations and, further, that that failure has the ultimate effect of rendering the U.S. insurer insolvent, it is very unlikely that the annuity obligations of the U.S. insurer would not be paid. The National Association of Life and Health Guaranty Associations (NOLHGA) reports that policyholders of insurance insolvencies between 1991 and 2009 have average recoveries of 96 percent on life claims and 94 percent on annuity claims.<sup>1</sup>

In addition, in 2016, NOLHGA published a Consumer Protection Comparison of the Federal pension system and the State insurance regulatory system. The State-based system of financial oversight of insurers is focused on preventing insolvencies and the early warning mechanisms that were enacted after 2008 have been even more effective in preventing insolvencies from happening in the first place. NOLHGA Comparison Report notes that since 2008, no operating annuity issuers with an active book of annuities had failed, and only a single former annuity issuer—Executive Life Insurance Company of New York, which had been in receivership since 1991—had been placed into liquidation. In that same period,

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<sup>1</sup> <https://www.nolhga.com/resource/code/file.cfm?ID=2984>

NOLHGA reports that 931 single-employer pension plans, affecting over 560,000 pension plan participants, failed.

**Q.3.** At the September 8 hearing, I asked you to identify what tools NAIC and regulators possess to address market failures. What can NAIC and/or State regulators do, if anything, to create coverage and capacity if insurers decide not to offer a particular coverage? What tools does NAIC have at its disposal, if any?

**A.3.** As State insurance regulators, our focus is on the dual objectives of protecting insurance consumers and ensuring competitive and stable markets in our States. If for some reason, consumers cannot obtain a particular coverage in their State (either because of the nature of the risk or the availability of the specific product they seek), a variety of mechanisms exist to secure coverage, depending on the kind of coverage. For example, the surplus lines market often provides coverage for risks that are difficult to place in the admitted market. Vehicular and property coverage would also be available through the State's residual market mechanism. We would encourage consumers that have difficulties with obtaining a particular coverage to contact their State's insurance department, which can seek to address such issues through appropriately tailored State-based regulatory solutions.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR TOOMEY  
FROM KATHLEEN A. BIRrane**

**Q.1.** *Private Equity in Insurance*—During the September 8th Banking Committee hearing, you noted that insurers owned by private equity firms are often subject to greater regulatory scrutiny than other insurance firms.

Please describe how regulatory treatment differs between private equity owned insurers versus insurers with more traditional ownership.

**A.1.** Any insurer, regardless of its ownership structure, is subject to our comprehensive regulatory regime that is experienced at both microprudential and macroprudential supervision. Our system focuses on risks at the individual insurer and group level, with extensive disclosure, analysis, capital requirements, and regulatory authority to protect solvency, while promoting product availability and affordability. Each form of ownership involves different potential risks for regulators to assess and mitigate as needed, as do different types of investments in the insurer's portfolio. Due to the recent increase in private equity owners, related party asset managers, and complexity of investments, we are reviewing existing guidance and considering updates and/or new requirements to ensure our ability to assess and address the risks to the insurers and their policyholders. The NAIC's Macroprudential Working Group has constructed a list of 13 specific regulatory considerations to ensure our ability to assess and address the risks to the insurers and their policyholders. This includes but is not limited to potential changes in the capital requirements for certain asset backed securities such as collateralized loan obligations, changes in the asset adequacy analysis testing requirements, and a review of several risks that are more common within private equity firms but that

may also be held by other insurers. This ongoing work will identify where existing disclosures, policies, affiliation requirements, and other controls and procedures should be modified, or new ones created, to address any gaps.

**Q.2. *Climate Financial Risk***—At the September 8th Banking Committee hearing, Senator Tester of Montana suggested that the U.S. is seeing 500-year events and 100-year events every decade and weather events are getting far worse. You stated “we know that weather patterns are changing and that those weather patterns are causing increased claims activity, et cetera. . . . You know, weather events are more frequent. They are more severe . . . .”

What data were you drawing from to support the assertion that climate related losses are getting worse?

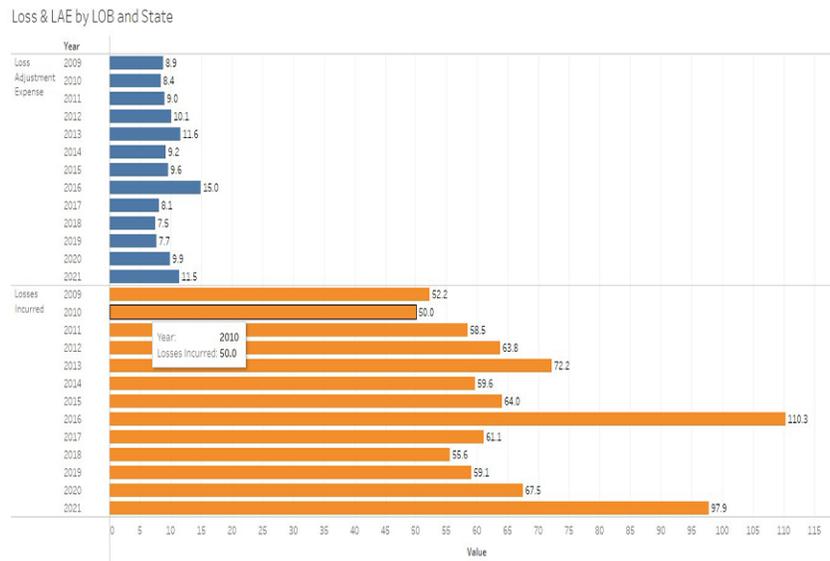
**A.2.** State insurance regulators are on the front lines of climate-related natural catastrophe preparedness and response, protecting policyholders and maintaining well-functioning insurance markets. For more than 150 years, State insurance regulators have experience and insight into the impact of climate-related risks on insurance and consumers.

The NAIC collects data from insurers to allow for regulatory analysis of climate risk including detailed quarterly and annual financial data from over 4,500 insurers, representing more than 98 percent of the premiums written in the U.S., as well as the collection of annual climate risk disclosure data from over 1,300 companies with 80 percent of the U.S. market captured by direct written premium.

Additionally, the NAIC collects loss data from insurers and through that data, you can see a correlation between extreme weather events and a spike in losses for the industry (See table below). Obviously, there are other factors at play, such as population sprawl and inflation, among other issues but those issues are only exacerbated by severe weather events. We measure the profitability of the industry on an annual basis and compare that against the U.S. Department of Commerce’s National Oceanic and Atmospheric Administration (NOAA) data regarding severe weather events.<sup>1</sup> According to NOAA, the 1980–2021 annual average of weather/climate disaster events with losses exceeding \$1 billion each is 7.7 events while the annual average for the most recent 5 years (2017–2021) is 17.8 events.<sup>2</sup>

<sup>1</sup> <https://www.climate.gov/news-features/blogs/beyond-data/2016-historic-year-billion-dollar-weather-and-climate-disasters-us>

<sup>2</sup> [https://www.ncei.noaa.gov/access/billions/#::text=In%202022%20\(as%20of%20October,events%20%20and%201%20wildfire%20event](https://www.ncei.noaa.gov/access/billions/#::text=In%202022%20(as%20of%20October,events%20%20and%201%20wildfire%20event)



**Q.3.** Roger Pielke, a prominent climate researcher who has testified before this Committee, argues that losses arising from extreme weather events are actually decreasing as a percentage of GDP even though coastal development has increased significantly.<sup>3</sup> Do you agree or disagree with his assessment? Please explain why.

**A.3.** The NAIC recognizes that a rigorous scientific process, one that is constantly evaluating and reevaluating data, assumptions, and outcomes, is beneficial to decision makers and ultimately creates better policies. The NAIC has no specific opinion on the research of Roger Pielke.

**Q.4.** Property insurers carefully manage risk associated with severe weather. If they fail to do so, they won't be in business very long. In your experience, do the firms you regulate effectively manage severe weather risks?

**A.4.** From the NAIC perspective, we have observed insurance industry efforts to manage risk associated with severe weather. The insurance industry is at the forefront of several collaborative efforts to reduce catastrophic risk. For example, through the property (re)insurers funding of the Institute for Business and Home Safety (IBHS), the insurance industry supports improved construction on, maintenance and preparedness practices. The IBHS conducts building safety and mitigation research to identify the most effective ways to create more resilient communities. Its research center in South Carolina is used to test how residential and commercial structures uphold against simulated weather events including hailstorms, windstorms, wind-driven rain, wildfires, and fires. It also

<sup>3</sup> Testimony of Dr. Roger Pielke, Jr., Professor of Environmental Studies at the University of Colorado before the U.S. Senate Committee on Banking, Housing, and Urban Affairs hearing entitled 21st Century Communities: Climate Change, Resilience, and Reinsurance. July 20, 2021. <https://www.banking.senate.gov/imo/media/doc/Pielke%20Testimony%207-20-21.pdf>

performs field testing in States with high exposure to tornadoes. The data gathered through its scientific research is then used to inform builders, homeowners, and businesses on disaster-resistant construction and mitigation practices. It also serves as the basis for IBHS's FORTIFIED national standards for resilient construction.

Additionally, insurers are collaborating with actuaries in order to identify their tail risk—the risk of how severe catastrophic losses could impair solvency. The Casualty Actuarial Society (CAS), the Canadian Institute of Actuaries (CIA), the Society of Actuaries (SOA), and the American Academy of Actuaries (AAA) began collaborating on research aimed at assessing climate risk and its potential risk implications to the insurance industry. As part of this effort, the group released a research paper entitled, “Determining the Impact of Climate Change on Insurance Risk and the Global Community”. The paper laid the framework for the development of the soon-to-be-released Actuaries Climate Index (ACI) and the Actuaries Climate Risk Index (ACRI).

These are a few examples of the many ways in which the insurance industry is working to manage its exposure to severe weather risks. The NAIC will continue to closely monitor these and other initiatives.

**Q.5.** Is risk management around severe weather something you monitor and regulate for?

**A.5.** Yes, State insurance regulators monitor and regulate for risk management and severe weather. This year, the NAIC's Climate and Resiliency Task Force facilitated revisions to the Climate Risk Disclosure Survey for participating States. The survey, which was first adopted by the NAIC in 2010, is a risk management disclosure tool for States to require of their insurers. These disclosures help insurance regulators assess and evaluate insurance industry risks and actions to mitigate climate risk. Currently, 15 States are participating in the survey with nearly 80 percent of the market captured by direct written premium.

As part of our insurance solvency regulatory framework, we collect information from insurers to monitor their exposures to both their underwriting and investment portfolios. Our State-based insurance regulatory system has developed an extensive set of tools to assess and analyze insurer's solvency and liquidity, and it is accustomed to adapting to an evolving risk landscape and is well-positioned to address the challenges presented by climate-related risks for insurers' underwriting, investments, and solvency. We have developed and implemented longstanding and well-established tools to address solvency concerns that incorporate exposure to climate-related catastrophes including the Own Risk and Solvency Assessment (ORSA), the Risk Based Capital (RBC) formula, and the NAIC's Financial Condition Examiner's Handbook. For example, in 2017, the NAIC expanded the risks quantified in the RBC formula to include a specific charge for hurricane and earthquake catastrophe risk in order to recognize increased exposure to catastrophic events. Most recently, the solvency workstream of the Task Force, which I chair, recommended that wildfires be added to the RBC framework for catastrophe risk exposures. In addition, based on the recommendations of our workstream and the Task

Force, the NAIC’s Financial Condition Committee is considering specific enhancements to the solvency oversight tools used by State insurance regulators that will expand the evaluation of an insurer’s exposure and response to climate-related financial risk, particularly in areas such as transition risk. The Task Force is also evaluating viable approaches to scenario analysis and stress testing for insurers as the data necessary to conduct such exercises becomes available.

Our detailed work to address climate-related risks in the insurance sector is highlighted in our letter to the U.S. Department of the Treasury regarding its request for information for its upcoming climate report.<sup>4</sup> The NAIC also issued a report titled, “Adaptable to Emerging Risks: The State Based Insurance Regulatory System is Focused on Climate-Related Risk and Resiliency”.<sup>5</sup>

**RESPONSES TO WRITTEN QUESTIONS OF  
SENATOR CORTEZ MASTO FROM KATHLEEN A. BIRrane**

**Q.1.** Insurance companies benefit from being members of Federal Home Loan Banks in two important ways: first, they receive significant dividend income, and second, they benefit from taxpayer-subsidized advances.

How do insurance companies use those advances?

**A.1.** How insurance companies use advances is specific to each insurer. Although insurers provide a narrative disclosure<sup>1</sup> on the use of funding, it is fairly limited. From a review of a few large insurance entities, they reference the use of funding as a source of “contingent liquidity” and for “spread margin/spread products/spread strategy.” Regulators, through their ongoing solvency oversight and via projects such as the NAIC Liquidity Stress Test (LST), have recognized the important role the FHLB serves for life insurers as a primary source of ad hoc liquidity needs.

**Q.2.** If they use those advances to invest in housing, is that affordable or market-rate housing?

**A.2.** Insurers are not required to, nor does the NAIC receive disclosure on the amounts of advances used for housing or the types of housing. Most advances are invested in fixed income securities, which may not necessarily be used to invest in housing related securities. Insurance company housing sector investments are typically comprised of investments in mortgage-backed securities, which is generally market rate housing.

**Q.3.** How is the public served by insurance companies’ membership in the Federal Home Loan Banks?

**A.3.** This question may be best addressed by the Federal Housing Finance Agency (FHFA). FHFA’s regulation on Federal Home Loan Banks membership specifies how and when an institution must

<sup>4</sup><https://content.naic.org/sites/default/files/testimony-letter-response-fio-rfi-climate-financial-risk-211111.pdf>

<sup>5</sup><https://content.naic.org/sites/default/files/climate-resiliency-resource-report-adaptable-emerging-climate-related-risk-resiliency-2021.pdf>

<sup>1</sup>Disclosures on FHLB activity are detailed in Statement of Statutory Accounting Principles (SSAP) No. 30, paragraph 18 (captured in Note 11 of the financial statements). These disclosures include narrative info on agreements, type of borrowing and use of funding, as well as data-captured information on FHLB stock, collateral pledged and borrowing information.

demonstrate compliance with each of the statutory membership eligibility requirements. An entity cannot qualify to be a member in the FHLB without investing in housing.

**Q.4.** Western States have experienced unprecedented wildfires, collectively costing the West \$21 billion annually.

Is a comparable program to the National Flood Insurance Program needed for fire and drought?

**A.4.** At this time, the NAIC has not taken a formal position on this issue.

**Q.5.** How can we increase fire mitigation on BLM land and other forested land overseen by the Federal Government to reduce threats of fire?

**A.5.** In 2020, the NAIC’s Center for Insurance Policy and Research (CIPR) along with Risk Management Solutions Inc. (RMS), and the Insurance Institute for Business and Home Safety (IBHS), released a paper called “Application of Wildfire Mitigation to Insured Property Exposure”.<sup>2</sup> Although this paper did not specifically address BLM land management, it did find that structural modifications can reduce wildfire risks up to 40 percent, and structural and vegetation modifications combined can reduce wildfire risk up to 75 percent when simply moving to a well-built wildfire-resistant structure from a neutral property setting. Avoided losses can be even more significant (e.g., 5 times greater) when compared to a highly flammable structure. From a benefit-cost perspective, the paper also demonstrated that for a number of modeled locations, the relative risk reduction, if enabled within insurance products based on wildfire risk-based pricing, would provide economically effective incentives at promoting mitigation with pay-back periods from 10 to 25 years.

**Q.6.** Municipal governments will face an increasing amount of humanitarian and financial strain as more—and more destructive—weather disasters occur.

What changes are insurance firms making—or need to make—to meet the needs of municipal government

**A.6.** The NAIC monitors insurance innovations in the climate risk and resilience space and serves as a forum where insurers, regulators, and other stakeholders can discuss their efforts to innovate and work collaboratively on climate resilience solutions. Through the NAIC’s Climate and Resiliency Task Force, State insurance regulators have heard from the insurance industry and their partners regarding community-based insurance efforts. For example, in 2021, the NAIC heard a presentation by Munich Reinsurance America Inc. and The Nature Conservancy regarding “Nature’s Remedy: Improving flood resilience through community insurance and nature-based mitigation”<sup>3</sup> that focused on coupling community-based insurance with mitigation projects, such as preserving or restoring floodplains and wetlands, implementing levee setbacks, and designing appropriate flood storage to emulate river flood pulse. We also heard from Marsh McLennan focusing on “Commu-

<sup>2</sup> <https://content.naic.org/sites/default/files/cipr-report-wildfire-mitigation.pdf>

<sup>3</sup> <https://content.naic.org/sites/default/files/national-meeting/Munich%20Re-Floodmitigationpaper.pdf>

nity-Based Catastrophe Insurance: One Method for Closing the Disaster Protection Gap”.<sup>4</sup> as an innovative mechanism to increase insurance coverage and enhance resilience. Specifically, insurance arranged by a local government or quasi-governmental body to cover a group or designated properties or individuals within the community’s jurisdiction. These are just two of the many ways insurance firms and municipalities can work together to address the effects of weather disasters.

**Q.7.** Will local governments continue to access comprehensive and affordable insurance coverage?

**A.7.** As State insurance regulators, we strive to maintain the critical balance between insurer solvency and reasonable rates, which can be challenging in certain areas that insurers view as presenting a greater risk of loss. As losses continue to rise, insurers must have enough funds to pay claims, making it critically important that we do what we can predisaster to mitigate the potential impacts of catastrophes. Risk reduction and mitigation can protect policyholders and reduce the losses paid by insurers—or otherwise absorbed through Federal spending—helping to maintain solvent insurance markets while keeping rates more affordable. Through the NAIC’s Climate and Resiliency Task Force, we have been working to help promote mitigation. The most vulnerable communities may benefit more from whole-community protection. Underserved communities are the least likely to have adequate insurance and the least likely to be able to afford mitigation retrofits, which is why resiliency funding is essential. For this reason, the Task Force is also exploring community-based solutions and working with States to identify resiliency funding programs and public–private capital frameworks.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARNOCK  
FROM KATHLEEN A. BIRRANE**

**Q.1.** I also believe that the United States has a strong and resilient insurance industry because of the comprehensive regulatory environment we have put in place. To ensure we can continue to successfully mitigate systemic risk, what tools do regulators have, or need, to properly supervise these transfers?

**A.1.** Over the past decade, State insurance regulators have made many enhancements to group supervision, informed by lessons from the financial crisis. We have expanded and strengthened our holding company statutes, implemented stronger corporate governance requirements, and now require larger insurers to file an Own Risk and Solvency Assessment (ORSA), which is a globally recognized report of all the risks posed to an insurance group, both from within the insurers, and from non-insurance affiliates regardless of their geographic location. Additionally, we have rolled out our Group Capital Calculation (GCC), giving regulators groupwide insight into capital allocation. Those improvements demonstrated their value over the last 3 years where even in the midst of historic market volatility and stress, the U.S. insurance sector proved to be financially strong and resilient.

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<sup>4</sup> <https://content.naic.org/sites/default/files/inline-files/GuyCarpenter-Presentation.pdf>

The NAIC's Insurance Holding Company System Regulatory Act and Insurance Holding Company System Model Regulation have historically provided State insurance regulators with the framework for insurance group supervision. In 2020, the NAIC adopted revisions to these models to create a GCC and Liquidity Stress Test (LST). The GCC adds another analytical tool to State insurance regulators' toolbox on group supervision. It assists regulators in holistically understanding the financial condition of non-insurance entities. It provides key financial information on the insurance group, quantifies risk across the insurance group, supports transparency into how capital is allocated, and aids in understanding whether and to what degree insurance companies may be supporting the operations of non-insurance entities. The GCC was built to strengthen State regulation, but it also serves to satisfy the group capital assessment requirements of the Covered Agreements with the EU and U.K.. The LST was developed to provide State insurance regulators with insights into a key macroprudential risk monitored by the Financial Stability Oversight Council (FSOC) and other jurisdictions internationally, but it also enhances group supervision. The LST requires insurers to file the results of a specific year's Liquidity Stress Test with the lead State insurance commissioner.

As noted in our testimony, State insurance regulators have also been actively monitoring the recent growth of alternative asset management companies, private equity (PE) firms among them, in the life insurance sector. The NAIC's Macroprudential Working Group has developed a list of 13 regulatory considerations related to their ability to adequately assess risks posed to insurers because of recent increases in the complexity of investments and other developments. This list is being used to identify where existing disclosures, policies and/or procedures should be modified, or new ones created, to address any gaps based on the increase in the number of PE owners of insurers as well as the increase in asset managers' involvement in insurance, the increase of private investments in insurers' portfolios, and other causes. We have extensive data reporting and analytical capability, to review and assess alternative investments or unique structures, and we are continuing to refine those tools as we speak. More specifics of this work are highlighted in our letter to Chairman Brown regarding his request for information on this issue.<sup>1</sup>

**Q.2.** Do you believe the insurance industry is ready or adequately taking into consideration the multitude of risk factors that climate change poses?

**A.2.** As State insurance regulators, we have long been committed to monitoring and addressing how climate risks impact policyholders and the insurance industry. We recognize the insurance sector is exposed to potential risks on the asset side of the balance sheet through their investments and on the liability side through the risks insurers underwrite. As part of our insurance solvency regulatory framework, we monitor their exposures to both their underwriting and investment portfolios. An important tool we use for monitoring climate-related risks is insurer climate disclosures

<sup>1</sup> <https://content.naic.org/sites/default/files/government-affairs-letter-naic-pe-response-sen-brown-220531.pdf>

which help insurance regulators assess and evaluate insurance industry risks along with insurer actions to mitigate climate risk. In 2010, the NAIC membership adopted the Insurer Climate Risk Disclosure Survey to identify trends, vulnerabilities, and best practices by collecting information about how companies assess and manage climate risk. As of 2021, 15 States are participating in the survey with nearly 80 percent of the market captured by direct written premium. Our detailed work to address climate-related risks in the insurance sector is highlighted in our letter to the U.S. Department of the Treasury regarding its request for information for its upcoming climate report.<sup>2</sup> The NAIC also issued a report titled, “Adaptable to Emerging Risks: The State Based Insurance Regulatory System is Focused on Climate-Related Risk and Resiliency”.<sup>3</sup>

**RESPONSES TO WRITTEN QUESTIONS OF SENATOR HAGERTY  
FROM KATHLEEN A. BIRrane**

**Q.1.** I have read reports that the NAIC has imposed a series of regulations that force insurance companies to obtain ratings from the SVO, rather than allowing insurance companies to obtain ratings from private-sector NRSROs for assets on their balance sheets.

Please detail the categories of securities and/or assets that the NAIC now requires an SVO designation and no longer recognizes ratings from private sector NRSROs? Please explain the rationale behind the NAIC SVO’s actions.

**A.1.** As a prudential regulator, State insurance regulators are empowered by State law to assign risk weights to insurer investments in order to support solvency. State regulators implement this function via the NAIC. The NAIC’s Valuation of Securities Task Force (VOS/TF), comprised of regulators, formulates and implements NAIC’s credit assessment and related policies. The Securities Valuation Office (SVO) is the professional staff assigned to support the VOS/TF. The SVO conducts credit quality assessments of securities owned by State-regulated insurance companies and performs such other duties specified by VOS/TF in the Purposes and Procedures Manual of the NAIC Investment Analysis Office (P&P Manual) or assigned by other NAIC regulator groups, from time to time. NAIC designations are intended for State regulators only and have the sole purpose of helping State insurance departments better identify the creditworthiness of insurance companies’ holdings and determine solvency risk.

As a default setting, all securities need to be filed with the NAIC. The filing process involves providing the NAIC with sufficient information so that we may assign a risk weight—a “designation” in NAIC parlance. However, there always have been large exceptions to this rule. The securities which do not need to be filed are called FE for “filing exempt.” Many large corporate and municipal obligations are FE if they have an NRSRO rating. Not all FE bonds require a NRSRO rating. For example, U.S. Govt securities as well as bonds issued with a full faith and credit guarantee of the U.S.

<sup>2</sup><https://content.naic.org/sites/default/files/testimony-letter-response-fio-rfi-climate-financial-risk-211111.pdf>

<sup>3</sup><https://content.naic.org/sites/default/files/climate-resiliency-resource-report-adaptable-emerging-climate-related-risk-resiliency-2021.pdf>

qualify for the lowest risk weight without the need for a NRSRO rating, State insurance regulators regularly move securities in and out of FE. For example, after NRSRO performance in the Global Financial Crisis, the regulators moved residential mortgage-backed securities from FE to NAIC modeled. More recently, credit-lease backed securities were moved from NAIC to FE. This process is ongoing and revolves around the regulators' supervisory priorities.

With regard to the specific questions, we have included a link to the P&P Manual <https://content.naic.org/sites/default/files/PPM-OSS-21.pdf>, which includes the policy on the use of credit ratings in Part One and the list of securities that are not eligible for Filing Exemption (the use of credit rating provider ratings) in Part Three. The NAIC uses credit rating provider credit ratings when it deems them appropriate for insurance company financial solvency regulation. We would be willing to discuss with you further to help in understanding the nature of our work and how NAIC policy comes about relative to reliance on NRSROs.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR MORAN  
FROM KATHLEEN A. BIRrane**

**Q.1.** One important line of insurance subject to robust State regulation is title insurance, which insures both homeowners that they own their properties free of undisclosed title defects and lenders that they have a valid lien on mortgaged collateral. NAIC's Title Insurance Task Force is the primary forum for State regulators to discuss and monitor impacts affecting consumers and the regulation of the title insurance industry.

At the direction of the FHFA, Fannie Mae and Freddie Mac (the Enterprises) recently released Equitable Housing Finance Plans, which announced an expansion to the use of attorney title opinion letters in lieu of proven, State-regulated title insurance, purportedly to lower real estate closing costs for low-to-moderate income borrowers. Some attorney opinions being offered in the marketplace claim to include an errors and omissions (E&O) insurance "wrapper" that makes the attorney opinion an "alternative" to title insurance.

However, there are a number of places, including in the growing area of fraud, for instance, where this "alternative" does not provide the comprehensive coverage that title insurance does—thus exposing consumers to both significant costs and risks to their property rights. I understand these products are being offered to both consumers (homeowners) and mortgage lenders, with some providers claiming to offer them in all 50 States.

I have concerns regarding the impact on homeowners and consumers in particular, and hoping NAIC can provide us with your perspectives on these issues as the public officials directly responsible for consumer protection under State insurance laws and the primary regulators of the insurance industry.

How are State insurance regulators approaching attempts to evade basic regulatory structures in place? In the aforementioned example, a surplus lines insurer seems to be attempting to offer an "alternative" to a traditional product to avoid the robust State regulatory model.

What is the NAIC doing to address concerns about products such as this one that purposely circumvent insurance regulatory oversight and pose significant consumer protection risks?

**A.1.** As State insurance regulators, protecting policyholders and addressing any unfair treatment of insurance consumers is crucial to the work we do and a bedrock principle of our regulatory framework. The NAIC’s Title Insurance Task Force, of which I am a member, is aware of the concerns that you have raised and will be hearing presentations on this issue at our NAIC Fall National Meeting in December 2022. We will keep the committee apprised of any developments.

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**RESPONSES TO WRITTEN QUESTIONS OF CHAIRMAN BROWN  
FROM STEVEN SEITZ**

**Q.1.** Insurers help policy holders deal with unexpected risk to their homes, their businesses, or their loved ones. Insurers assume this risk in the hope that premiums will generate profits—or return on capital. When excessive risk is taken, policy holders and the entire economy can be at risk. Reinsurance—the practice of transferring risk to others—can pose a threat to policy holders and annuitants and is seen as a potential blind spot for regulators as some firms have as much as 80 percent of their obligations placed with offshore reinsurers. That can mean hundreds of thousands of workers and families facing increasing risks when insurers hold less capital and there is little or no transparency about where those assets are held. Are there loopholes in existing regulations that create opportunities for insurers to use offshore reinsurance deals to either hold less capital or load up on riskier investments?

**A.1.** Response not received in time for publication.

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**RESPONSES TO WRITTEN QUESTIONS OF SENATOR TOOMEY  
FROM STEVEN SEITZ**

**Q.1.** *Private Equity Workstream*—At the September 8th Banking Committee hearing, I asked you if you are involved in an effort to make recommendations to the International Association of Insurance Supervisors (IAIS) regarding private equity’s involvement in insurance. You failed to adequately respond to my question about your involvement in this matter.

In your capacity as Director of the Federal Insurance Office (FIO), you are a member of the executive committee of IAIS. In an August 12, 2022, meeting of the National Association of Insurance Commissioners (NAIC) Financial Stability Task Force and the Macroprudential Working Group, it was reported that the IAIS formed a Private Equity Workstream “to produce an internal briefing memo to the Macroprudential Committee that provides an update on the involvement of PE in members’ jurisdictions.”<sup>1</sup> It was also reported that the Macroprudential Supervision Working Group

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<sup>1</sup>National Association of Insurance Commissioners, Financial Stability (E) Task Force and Macroprudential (E) Working Group Meeting Minutes. <https://content.naic.org/sites/default/files/nationalmeeting/Minutes-FSTF.pdf> Pp. 7–8.

will continue to monitor private equity ownership in the global insurance industry.<sup>2</sup>

Are you or anyone else from the Treasury Department involved with the Private Equity Workstream that was formed by IAIS?

Have you or anyone else from the Treasury Department contributed information that may or may not be used for this internal briefing memo to the Macroprudential Committee?

Can you commit to providing this Committee any briefing memos or other final documents developed as a part of the Private Equity Workstream? If not, please explain why.

**A.1.** Response not received in time for publication.

**RESPONSES TO WRITTEN QUESTIONS OF  
SENATOR CORTEZ MASTO FROM STEVEN SEITZ**

**Q.1.** Insurance companies benefit from being members of Federal Home Loan Banks in two important ways: first, they receive significant dividend income, and second, they benefit from taxpayer-subsidized advances.

How do insurance companies use those advances?

If they use those advances to invest in housing, is that affordable or market-rate housing?

How is the public served by insurance companies' membership in the Federal Home Loan Banks?

**A.1.** Response not received in time for publication.

**Q.2.** Western States have experienced unprecedented wildfires, collectively costing the West \$21 billion annually.

Is a comparable program to the National Flood Insurance Program needed for fire and drought?

How can we increase fire mitigation on BLM land and other forested land overseen by the Federal Government to reduce threats of fire?

**A.2.** Response not received in time for publication.

**Q.3.** Municipal governments will face an increasing amount of humanitarian and financial strain as more—and more destructive—weather disasters occur.

What changes are insurance firms making—or need to make—to meet the needs of municipal government?

Will local governments continue to access comprehensive and affordable insurance coverage?

**A.3.** Response not received in time for publication.

**RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARNOCK  
FROM STEVEN SEITZ**

**Q.1.** What are some benefits and drawbacks of the U.S. system of insurance regulation being primarily based at the State level?

**A.1.** Response not received in time for publication.

**Q.2.** Would you describe some discussions you've had with State regulators or stakeholders surrounding the disruptions they expect

<sup>2</sup> Ibid.

as a result of climate change and how these approaches differ by region?

**A.2.** Response not received in time for publication.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD  
**LETTER SUBMITTED BY THOMAS D. GOBER, INSURANCE AND  
REINSURANCE FRAUD EXPERT**

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September 13, 2022

The Honorable Sherrod C. Brown, Chairman  
Committee on Banking, Housing and Urban Affairs  
503 Hart Senate Office Building  
Washington, DC 20510

Chairman Brown,

The Senate Banking committee's effort to understand the build-up of financial risk within the state-regulated life/annuity (L&A) industry will not necessarily be easy, but I believe that you are performing an urgent public service. Too many for-profit life/annuity companies are using regulatory arbitrage to circumvent statutory accounting rules in ways that raise the enterprise-level and systemic risks in their industry as well as in the interconnected financial system.

I am a Certified Fraud Examiner and forensic accountant. For 37 years, I have sought to protect insurance policyholders and contract owners. I began serving as an insurance examiner in 1985. After accreditation and certification, I served as state examiner-in-charge for the state of Mississippi.

In 1990, I began assisting the US Department of Justice and the Federal Bureau of Investigation in criminal investigations in a variety of capacities, including covert and overt work, and consulting and testifying as an expert. My work with the US DOJ spanned more than ten years, during which time every case we worked was successful. In addition to lengthy prison sentences for the executives, we got the funds back for policyholders through forfeiture under criminal RICO. More recently I have assisted groups of agents, advisers, and fiduciaries, conducting deep dive analyses of L&A insurers' financial viability and transparency.

In the course of my work, I have become concerned about high-risk and low transparency practices in the L&A industry, by individual companies and across the industry, that I believe are adding stress to the liquidity and solvency of the entire industry. My concerns, which others in my field share, reflect these issues:

- Reinsurance Ceded to U.S. Captives and Offshore Jurisdictions to Reduce Transparency and Disguise Less-Than Arm's-Length Transactions
- The Use of Non-Admitted Assets, Such as Letters of Credit and Credit-Linked Notes
- Escalation and Concentration of High-Risk, Low-Liquidity Investments Relative to Surplus

□ **Increased Leverage and Risk of a ‘Run-on-the-Bank’ Through the Sale of Funding Agreements**

State insurance regulators have not sufficiently questioned the increasingly global L&A industry about these issues, in my opinion. They hesitate to do so even as certain insurers in that industry have vastly expanded their balance sheets while minimizing their surpluses. This mode of expansion may amplify enterprise-level as well as systemic risk. In my professional opinion, the L&A industry is too large and complex for a state-based regulatory system which includes many state agencies which are underfunded and understaffed. The state regulators have evolved away from a cohesive - level playing field - network to what now includes an increasing number of states that are permitting their captives to make a mockery of an otherwise rock-solid set of NAIC statutory accounting fundamentals and Holding Company Act.

More aggressive inquiry into the recent practices of this regulated but opaque and rapidly evolving industry is overdue, I believe. State insurance regulators may not welcome what they perceive as interference in their jurisdictions. But industries can outgrow their regulators, and even the best oversight bodies can benefit from oversight. Thank you for this opportunity to share my professional experience with your committee. After you have had an opportunity to review this information and related exhibits, please do not hesitate to reach out to me for additional information or clarity.

**I. Reinsurance Ceded to Captives and Offshore Jurisdictions to Reduce Transparency and Disguise Less-Than Arm’s-Length Transactions**

[See Exhibit A]

**U.S. Captives**

The NAIC Model Holding Company Act requires that material transactions between regulated insurance companies and any affiliate be “fair and reasonable” and that the records “of each party shall be so maintained as to clearly and accurately disclose the nature and details of the transactions.” Yet, the U.S.-based captives appear to have been invented and structured to avoid those fundamentals.

For several years, a growing number of US life/annuity insurers have been setting up affiliated reinsurers and SPVs in certain jurisdictions in order to reinsure hundreds of billions of dollars in annuity and life insurance liabilities. I estimate that for-profit (and a few mutual and no fraternal) life insurers in the US have ceded more than \$400 billion in liabilities to captive reinsurers over the past two decades.

Most of these liabilities are future long-term financial obligations to policyholders, contract owners, and US retirees—in other words, their savings.

Such jurisdictions give special treatment to captives domiciled in their state. Capital requirements are lower than insurers, investment limitations virtually non-existent and transparency is minimal to zero.

While captives use a variety of different mechanisms (like using LOCs or Parental Guarantees), the net effect of the insurer-captive relationship is designed to permit the insurer to fund significantly less of the obligations to policyholders/contract owners than the insurer is required under U.S. SAP.

When executed properly, reinsurance transactions are not problematic. Legitimate reinsurance can be an effective tool in spreading risk. When the counter-parties—ceding insurer and reinsurer—are separate companies, with independent sources of capital and independent teams of actuaries, accountants, and attorneys, reinsurance can be a valuable tool. In other words, when the transactions are “arm’s-length” and each party protects its own interests, the ceding company truly has a backstop from a well-informed and well-capitalized reinsurer.

But when the insurer and reinsurer are owned by the same holding company, auditors and regulators can make no presumption of arm’s-lengthness. That is why the NAIC had to require all states to adopt their Model Holding Company Act; to impose fairness and reasonableness and alleviate self-dealing.

When L&A companies first began using these captives, around 2000, they started with small amounts that attracted little attention. In 2009, however, an unusual number of new reinsurance companies were formed in Vermont and South Carolina. When, on behalf of a client, I asked for the annual statements of those new reinsurers, they weren’t available. The captives do not file public annual statements.

That was extraordinary. All insurance and reinsurance companies domiciled in the US must file annual sworn statements. Despite the lack of access, my colleagues and I have been able to piece together, through various footnotes of insurers’ audit reports and industry articles, the captive reinsurers’ use of several practices that are expressly prohibited by the NAIC Statutory Accounting Principles (SAP).

It is my professional opinion that a regulated US L&A insurer should not be allowed to cede business to a U.S. captive or an offshore reinsurer that is not required to comply with U.S. SAP. To do so creates an immediate and false inflation of viability. I am not alone in this expectation. When the NAIC became concerned about the misuse of captives by the L&A industry, they published a white paper dated June 6, 2013, to specifically address these opaque captives. In their opening introductory paragraph, they state “Commercial insurer-owned captives and SPVs should *not be used to avoid* statutory accounting.” [Emphasis added]

Numerous articles and research papers have expressed the same concerns, questioning why these arrangements can enable significant underfunding when the liabilities (promises to pay policyholders) are the exact same, despite having been “moved” to Vermont or Arizona, Bermuda or Malta.

#### **Bermuda, Cayman and other Offshore Reinsurance Locations**

All of the examples above related to captive reinsurers domiciled in states in the US that allow reinsurers to avoid SAP, despite the NAIC's stated intention. In this section we will address how life/annuity insurers use captive insurers in offshore locations such as Bermuda or the Cayman Islands for similar purposes.

Distribution and marketing expenses are a significant burden for companies selling annuities; they must pay wholesalers and insurance agents first-year commissions and fees ranging up to 10%. If a life/annuity company acquires \$1 billion in annuity premium, it might have paid \$50 million to \$100 million in so-called acquisition costs.

Under SAP in the US, the acquisition costs must be expensed in the same year they are paid—the money is spent and unavailable to pay claims. But a reinsurer using GAAP in Bermuda, or the Cayman Islands can defer (Deferred Acquisition Costs – DAC) the expense over the life of the annuity, diluting its actual impact on the reinsurer's surplus. Industry insiders have shared that this practice of making use of these disparate accounting regimes has a verb and adjective form in insurer home offices - known as "DACable" and "DACability" and may be more useful/applicable when ceding closed block business than recurring, but it can be used to shore up the reinsurer's financial appearance even when flow arrangements to the reinsurer are involved.

The surplus looks larger than it is, and the company appears to have more free capital than it actually does. Executive management of the offshore reinsurer are free to do virtually anything with the extra funds.

#### **II. The Use of Non-Admitted Assets, Such as Letters of Credit and Credit-Linked Notes**

A life/annuity company sells contracts that involve long-term commitments. To ensure long-term solvency, they maintain buffers or surpluses. These cushions absorb declines in asset values and/or increases in estimated liabilities. But the companies must hold assets whose values are firm and subject to regulatory review, and the estimates of their liabilities must be duly conservative.

Earlier, I mentioned that transferring liabilities to captive reinsurers appears to reduce the estimated cost of those liabilities, in terms of required capital. Now I'd like to talk about firms' use of captive reinsurers to back their liabilities with assets that would not be admitted by examiners in their own domiciles.

In certain captive-friendly jurisdictions (including VT, SC, AZ), a captive can post Letters of Credit, Parental Guarantees, Credit-Linked Notes and various other contingent instruments as Admitted Assets, despite the fact that both SAP & GAAP disallow such contingent instruments.

These actions add to the leverage of the reinsurer in ways that are invisible to the public and obscure even to regulators—until the leverage levels become unstable. Understanding the fundamentals of why some instruments shouldn't be booked as admitted assets is essential to recognizing how non-compliant these captive mechanisms are.

The NAIC clearly describes this necessity of conservatism (from the Preamble to the NAIC Accounting Practices & Procedures Manual):

[See Exhibit B]

To ensure that life insurers comply with the reasonably conservative accounting practices and to provide a level playing field across all 50 states, the NAIC Accounting Practices & Procedures Manual (APPM) includes Statements of Statutory Accounting Principles (SSAP).

Arguably, the most fundamental SSAP upon which an insurer's balance sheet is built is SSAP No. 4, Admitted Assets:

[See Exhibit C]

My objection is that Letters of Credit (LOC) are contingent on an event or multiple events. Until the event has occurred, its *contingency* prevents it from even being defined as an asset, much less be deemed an *admitted* asset. Contingency means that a particular event (or multiple events) must occur before the LOC can be drawn upon.

For example, an insurer might cause its captive to arrange for an LOC from a bank. The LOC, similar to a line of credit, might have a potential value of \$1 billion but cost the captive only a \$50 million fee to establish it. Should the captive book the LOC as a \$1 billion asset or as a \$50 million expense?

An insurance examiner in the US would not admit it as an asset. Why? Because the LOC is analogous to a \$2 lottery ticket that has a chance to win \$300 million. An insurance examiner should, in my opinion, record the ticket as a \$2 expense, not as a \$300 million asset—because the \$300 million valuation is contingent on holding the winning ticket.

Yet US life insurers are using their captive reinsurers, and the rules of the haven in which it purposely domiciled the reinsurer, to avoid prohibitions under SAP against booking letters of credit as assets at their face value.

Credit Linked Notes (CLNs) raise the same types of concerns. A CLN is a security with an embedded credit default swap permitting the issuer to shift specific credit risk to credit investors. CLNs are typically created through a special purpose vehicle (SPV), or trust, which is collateralized with AAA-rated securities.

In a situation I am currently reviewing, a L/A insurer owns two captive reinsurers that are domiciled in Delaware. The Delaware auditors recently admitted \$3.8 billion worth of CLNs as assets, allowing the reinsurers to credit that amount to their surpluses. In a state filing, the parent admitted that, "If our subsidiaries had not been permitted to include the CLNs in surplus, our subsidiaries' risk-based capital (RBC) would have triggered a regulatory event."

These types of practices increase the insurers' leverage levels in unseen ways, and, because of the interconnectedness of life insurers, increases the fragility of the financial system.

[See Exhibit D]

### III. Escalation and Concentration of High-Risk, Low-Liquidity Investments Relative to Surplus

I would like to introduce a simple ratio that the insurance industry, regulators and ratings agencies use to broaden their calculation of risk: The ratio of *risky* assets to *total* Surplus. We believe that this ratio is important and should be used to benchmark the strength of life/annuity insurers.

In the last decade, L&A insurer assets have skyrocketed. While many companies have departed the annuity industry since the Great Financial Crisis of 2008, several new and existing carriers have grown dramatically through mergers and assumptions of large blocks of insurance, individual annuities, and group annuities (in transactions known as pension risk transfers, or PRT).

With rising sales of annuities, life insurer liabilities have also surged. Many companies report razor-thin surpluses relative to the size and risk profile of their balance sheets. For instance, a leading annuity issuer, Athene Annuity & Life Company (AALC), at 12/31/2021, reported total surplus of \$1.28 billion and total assets of \$106.3 billion, a ratio of only about 1.2%.

One of the highest risk categories in the NAIC annual statement is "Other loan-backed and structured securities." It is separate from Residential Mortgage-Backed and Commercial Mortgage-Backed Securities and includes asset-backed categories such as student loans, credit card debt and collateralized loan obligations (CLOs), which are securities backed by bundles of high-yield commercial loans.

For 2021, AALC reported "Other loan-backed and structured securities" in the amount of more than \$16.6 billion. Athene's assets in just this one high-risk category represent 15.56% of its total assets. But they represent **1,300% of its surplus**, a ratio we regard with great concern. In other words, if Athene's "other loan-backed and structured securities" lost only 8% of their value in a market crisis, the loss would wipe out Athene's surplus rendering it insolvent.

#### IV. Increased Leverage and Risk of a 'Run-on-the-Bank' Through the Sale of Funding Agreements

In recent years, for-profit life & annuity carriers have added to their leverage by selling notes backed by funding agreements, or "funding agreement-backed notes" (FABNs). According to Fitch Ratings, "Insurers writing FAs benefit by investing the proceeds in higher-yielding assets that are typically both cash flow and duration matched to the FABN. FABNs typically attract a diverse pool of potential investors that benefit from enhanced returns and a claims priority, which ranks *pari passu* with general account policyholders of the FA issuer.

Insurers obtain legal opinions that these funding agreements are treated *pari passu* with other insurance obligations. In other words, the lenders are on an equal footing with policyholders and contract owners.

In recent years, these FA borrowings sometimes exceed up to 3 times a life insurer's annual sales of all its life and annuity products. In a liquidity crisis, insurers may have to decide whether to fulfill their obligations to policyholders/contract owners, most of which are long-dated, or their funding agreement lenders. The professional investors (banks, insurance companies and other institutions) who buy funding agreements are more attuned to market signals than policyholders and annuity contract owners. They are better equipped to detect an impending liquidity crunch. They would likely request their funds long before policyholders and state regulators react.

Our concern is that, in a credit crisis, the life/annuity companies will first pay back their institutional investors (by selling their most liquid investments) and then fund policyholder/contract owner redemptions (by selling higher-risk, less liquid investments). In any case, highly leveraged life/annuity companies are vulnerable to liquidity crises, falling asset values, panicked creditors and forced sales of assets—doing potential damage to the economy at large.

In 2015, Federal Reserve researchers warned of potential illiquidity pressures that could lead to a "run on the bank" in the life and annuity industry by short-term creditors. Rather than heed the warnings, many of the for-profit L/A insurers subsequently increased their liability gathering through product sales. Another important point raised by the research paper is that by treating the funding agreements as insurance products, the insurer's typical measure of leverage is distorted.

See "Self-fulfilling Runs: Evidence from the U.S. Life Insurance Industry," Finance and Economics Discussion Series, Divisions of Research & Statistics and Monetary Affairs, Federal Reserve Board, Washington, DC, 2015).

#### Summary

I thank the committee for hearing my testimony. The subject matter is complicated, but the general concern can be described in two words: Regulatory Arbitrage.

The most significant issues that I believe are inadequately regulated and virtually unknown to the consumer include:

- Reinsurance Ceded to U.S. Captives and Offshore Jurisdictions to Reduce Transparency and Disguise Less-Than Arm's-Length Transactions
- The Use of Non-Admitted Assets, Such as Letters of Credit and Credit-Linked Notes
- Escalation and Concentration of High-Risk, Low-Liquidity Investments Relative to Surplus
- Increased Leverage and Risk of a 'Run-on-the-Bank' Through the Sale of Funding Agreements

Where there is any lack of transparency in a regulated, financial services industry, we can no longer be sure of a life insurer's true financial condition. "Trust but verify." In today's life/annuity industry, we would like to trust, but too often we cannot verify. An ERISA fiduciary who takes her duty very seriously suggested we should "Verify, then trust."

One additional point that several witnesses made to the committee was that the state guaranty associations act as a backstop in the event of an insurer's failure. I've learned through interactions with policyholders and professionals alike that they do not understand that, unlike the FDIC and PBGC, state guaranty associations are not prefunded and must retroactively assess solvent insurers to fill the hole left by the failed insurers. Presumably, the assessments would be passed along to policyholders as higher premiums.

I've spent 37 years and thousands of interviews with policyholders. Our U.S. citizens, even the brightest and best informed, have no idea about sleight-of-hand reinsurance or hidden leverage. They tell me all they can do is timely pay their premiums and trust someone is looking after them. What is mind boggling is that while a few honest and concerned industry insiders have confirmed all my suspicions addressed above, and worse, have said most industry insiders know the truth, publicly they remain silent.

We've seen this before. In the several years leading up to the 2008 debacle, while whistleblowers' timid cautions were shunned and dismissed, the industry and the ratings agencies they hired doubled down. The crucial point I am trying to make here is that unlike bank customers' deposits, policyholders have timely paid premiums for lifetimes in return for long-term promises. Every penny in these now sprawling, opaque holding company systems can be traced back to those policyholders. Mathematically we have moved from a watch to a warning. If a state regulator gives a nod to one of the highest-risk, lowest liquidity, thinnest surplus and least transparent life insurers in the country and the ratings agency assigns that insurer an A+ rating, the current regulatory system needs your prompt oversight and assistance.



Exhibit A

**INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT****Table of Contents**

Section 1.	Definitions
Section 2.	Subsidiaries of Insurers
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Section 15.	Judicial Review, Mandamus
Section 16.	Conflict with Other Laws
Section 17.	Separability of Provisions
Section 18.	Effective Date
Appendix.	Alternate Provisions

**Section 1. Definitions**

As used in this Act, the following terms shall have these meanings unless the context shall otherwise require:

- A. "Affiliate." An "affiliate" of, or person "affiliated" with, a specific person, is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.
- B. "Commissioner." The term "commissioner" shall mean the insurance commissioner, the commissioner's deputies, or the Insurance Department, as appropriate.

**Drafting Note:** Insert the title of the chief insurance regulatory official wherever the word "commissioner" appears.

- C. "Control." The term "control" (including the terms "controlling," "controlled by" and "under common control with") means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract other than a commercial contract for goods or nonmanagement services, or otherwise, unless the power is the result of an official position with or corporate office held by the person. Control shall be presumed to exist if any person, directly or indirectly, owns, controls, holds with the power to vote, or holds proxies representing, ten percent (10%) or more of the voting securities of any other person. This presumption may be rebutted by a showing made in the manner provided by Section 4K that control does not exist in fact. The commissioner may determine, after furnishing all persons in interest notice

## Insurance Holding Company System Regulatory Act

is disallowed. In the event of disallowance, the disclaiming party may request an administrative hearing, which shall be granted. The disclaiming party shall be relieved of its duty to register under this section if approval of the disclaimer has been granted by the commissioner, or if the disclaimer is deemed to have been approved.

- L. Enterprise Risk Filing. The ultimate controlling person of every insurer subject to registration shall also file an annual enterprise risk report. The report shall, to the best of the ultimate controlling person's knowledge and belief, identify the material risks within the insurance holding company system that could pose enterprise risk to the insurer. The report shall be filed with the lead state commissioner of the insurance holding company system as determined by the procedures within the Financial Analysis Handbook adopted by the National Association of Insurance Commissioners.
- M. Violations. The failure to file a registration statement or any summary of the registration statement or enterprise risk filing required by this section within the time specified for filing shall be a violation of this section.

**Section 5. Standards and Management of an Insurer Within an Insurance Holding Company System**

- A. Transactions Within an Insurance Holding Company System
  - (1) Transactions within an insurance holding company system to which an insurer subject to registration is a party shall be subject to the following standards:
    - (a) The terms shall be fair and reasonable;
    - (b) Agreements for cost sharing services and management shall include such provisions as required by rule and regulation issued by the commissioner;
    - (c) Charges or fees for services performed shall be reasonable;
    - (d) Expenses incurred and payment received shall be allocated to the insurer in conformity with customary insurance accounting practices consistently applied;
    - (e) The books, accounts and records of each party to all such transactions shall be so maintained as to clearly and accurately disclose the nature and details of the transactions including such accounting information as is necessary to support the reasonableness of the charges or fees to the respective parties; and
    - (f) The insurer's surplus as regards policyholders following any dividends or distributions to shareholder affiliates shall be reasonable in relation to the insurer's outstanding liabilities and adequate to meet its financial needs.
  - (2) The following transactions involving a domestic insurer and any person in its insurance holding company system, including amendments or modifications

**Exhibit B**

## Statutory Accounting Principles Preamble

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Interpreted by: INT 00-20

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### I. Accounting Practices and Procedures Promulgated by the NAIC

1. The NAIC, through its committees and working groups, facilitates many projects of importance to the insurance regulators, industry, and users of statutory financial information. That is evidenced by the mission statement and charges of the NAIC Accounting Practices and Procedures Task Force of the Financial Condition (E) Committee (Accounting Practices and Procedures (E) Task Force).

2. The mission of the Accounting Practices and Procedures (E) Task Force is to identify, investigate and develop solutions to accounting problems with the ultimate goal of guiding insurers in properly accounting for various aspects of their operations and to modify the NAIC *Accounting Practices and Procedures Manuals for Property and Casualty Insurance Companies, for Life, Accident and Health Insurance Companies, and for Health Maintenance Organizations* (Accounting Practices and Procedures manuals) to reflect changes necessitated by task force action and to study innovative insurer accounting practices which affect the ability of regulators to determine the true financial condition of insurers.

3. To carry out the mission, the Accounting Practices and Procedures (E) Task Force is charged with carrying out the following initiatives:

- Provide authoritative guidance to insurance regulators on current statutory accounting issues.
- Continue evaluation of statutory accounting principles for purposes of development, expansion and codification.
- Extend evaluation of statutory accounting principles to address areas specific to health entities.
- The Codification of Statutory Accounting Principles (E) Working Group (Statutory Accounting Principles (E) Working Group as of January 1, 2000) will maintain codified statutory accounting principles by providing periodic updates to the guidance which address new statutory issues and new generally accepted accounting principles (GAAP) pronouncements as they develop.

4. This comprehensive guide to Statutory Accounting Principles, composed of the Preamble, the Statements of Statutory Accounting Principles (SSAPs), and the Appendices, is intended to respond to the initiatives noted above. The guide and interpretations of the Emerging Accounting Issues (E) Working Group shall be referred to as the Accounting Practices and Procedures Manual - version effective January 1, 2001 (during the transition period until the 1998 version is no longer maintained and updated by the NAIC). The 1998 version of the Accounting Practices and Procedures Manual will be maintained and published until December 31, 2000. However, this Manual is not intended to preempt states' legislative and regulatory authority. It is intended to establish a comprehensive basis of accounting recognized and adhered to if not in conflict with state statutes and/or regulations, or when the state statutes and/or regulations are silent.

**Preamble**

5. The principles established by this Manual are effective January 1, 2001. Accounting changes adopted to conform to the provisions of these statements shall be reported as adjustments to unassigned funds (surplus) in the period of the change in accounting principle; however, specific effective dates, and transition or grandfathering rules, if any, are contained in each SSAP.

**II. Background**

**A. An Accounting Environment for Insurance Companies**

6. Accounting is the process of accumulating and reporting financial information about an economic unit or group of units. Relative to commercial enterprises, the users of accounting information include management, investors, potential investors, lenders, investment analysts, regulators, and customers. Although customers of most commercial enterprises have no direct financial interest therein and generally are only concerned with the price to be paid for the product or service purchased, they may use accounting information to make choices as to the entity with which they engage in a business transaction. This is particularly relevant to purchases of insurance products inasmuch as insurance contracts involve a promise to pay which may extend years into the future. Insurance products may provide benefits well in excess of the purchase price or premium. The benefits ultimately received are almost always greater than the price (premium) paid and can only be estimated at the time the product (policy) is purchased.

7. Insurance is regulated on a state by state basis in the United States. Each state has its own regulatory framework generally led by an insurance commissioner. Insurance commissioners are charged with overseeing the financial condition of insurance companies doing business in their jurisdictions and they require meaningful financial, statistical, and operating information about the companies. This financial oversight is designed to help ensure that policyholders and claimants receive the requisite benefits from the policies sold, often times such products having been sold years or decades prior to when the benefits are due. Frequently, this regulatory perspective differs markedly from the perspectives of other users of insurers' accounting information. In recognition of these special concerns and responsibilities, statutory accounting principles have been established by statute, regulation, and practice.

**B. Statutory Accounting Principles (SAP)**

8. In simplest terms, SAP has been those accounting principles or practices prescribed or permitted by an insurer's domiciliary state. Statutory accounting practices have been interspersed in the insurance laws, regulations, and administrative rulings of each state, the Accounting Practices and Procedures manuals, the Annual Statement Instructions, the NAIC *Financial Condition Examiners Handbook*, the *Purposes and Procedures Manual of the NAIC Securities Valuation Office*, and NAIC committee, task force, and working group minutes. In addition, there are many statutory practices widely accepted by both insurers and regulators which have never been codified.

9. SAP is conservative in some respects but not unreasonably conservative over the span of economic cycles, or in recognition of the primary statutory responsibility to regulate for financial solvency. SAP attempts to determine at the financial statement date an insurer's ability to satisfy its obligations to its policyholders and creditors.

**C. Comparison Of GAAP And SAP**

10. The objectives of GAAP reporting differ from the objectives of SAP. GAAP is designed to meet the varying needs of the different users of financial statements. SAP is designed to address the concerns of regulators, who are the primary users of statutory financial statements. As a result, GAAP stresses measurement of emerging earnings of a business from period to period, (i.e., matching revenue to expense), while SAP stresses measurement of ability to pay claims in the future. This difference is illustrated by the fact that statutory policy reserves are intentionally established on a conservative basis emphasizing the long-term nature of the liabilities. Under GAAP, the experience expected by each

**Preamble**

company, with provision for the risk of adverse deviation, is used to determine the reserves it will establish for its policies. GAAP reserves may be more or less than the statutory policy reserves.

11. Some other differences between SAP and GAAP have included:

- GAAP has recognized certain assets which, for statutory purposes, have been either nonadmitted or immediately expensed. Policy acquisition costs are expensed as incurred under SAP since the funds so expended are no longer available to pay future liabilities. Insurance company financial statements prepared in accordance with GAAP defer costs incurred in the acquisition of new business and amortize them over the premium recognition period.
- Deferred income taxes have, historically, not been recognized under SAP.
- The methods of accounting for certain aspects of reinsurance under GAAP may have varied from SAP, e.g., credit for reinsurance in unauthorized companies.

**D. Purpose of Codification**

12. The purpose of the codification of statutory accounting principles is to produce a comprehensive guide to SAP for use by insurance departments, insurers, and auditors. Statutory accounting principles, as they existed prior to codification did not always provide a consistent and comprehensive basis of accounting and reporting. The prescribed or permitted statutory accounting model resulted in practices that could have varied from state to state. Insurance companies were sometimes uncertain about what rules to follow and regulators were sometimes unfamiliar with the accounting rules followed by insurers in other states. As a result, insurers' financial statements were not always prepared on a comparable basis.

13. In engaging this project, it was necessary to revisit principles that had been developed over a long period of time and to consider recently identified accounting issues not currently addressed by SAP. In many cases, previously available choices of accounting methods were eliminated. Also considered was the current state of the regulatory environment and the tools more recently developed, such as risk-based capital (RBC). These new financial analytical tools allowed for a reconsideration of the level of conservatism necessary to achieve regulatory objectives.

14. The Codification project will result in more complete disclosures and more comparable financial statements, which will make the insurance departments' analysis techniques more meaningful and effective. The project will provide examiners and analysts with uniform accounting rules against which companies' financial statements can be evaluated. RBC, an important tool used by the states to measure solvency of insurers, will be reported more consistently with the benefit of codification.

**E. History of Codification**

15. In 1989, the NAIC adopted a Solvency Agenda designed to enhance the ability of state regulators to protect insurance consumers from the financial trauma of insurer insolvency. In recognition of the fact that enhancement of solvency regulation is an ongoing process, the agenda was updated in 1991. Since 1991, most major initiatives of the 1991 Solvency Agenda have been accomplished. They include: 1) revision of the NAIC *Financial Condition Examiners Handbook*, 2) development of a risk-based capital approach to define required levels of capital and surplus, 3) development of a model law on authorized insurer investments, 4) creation of a centralized financial analysis unit to perform comprehensive analysis of insurance companies who may be troubled, 5) development of computerized analytical routines for use by state insurance departments, and 6) creation of an NAIC education fund.

**Preamble**

16. The codification project is also a direct result of the 1991 Solvency Agenda. The goal was “evaluation of existing statutory accounting principles as presently outlined in the Accounting Practices and Procedures Manual for purposes of further development, expansion, and codification.”

17. Beginning in 1994, the NAIC’s efforts to codify SAP were strengthened and reorganized recognizing the need for expediency. There was both a commitment of substantial financial resources as well as the selection of a team of dedicated regulators who were willing to commit the time and effort necessary to accomplish one of the most significant undertakings that has been faced by the NAIC.

18. Recognition of this effort was given by the AICPA when in 1995 they issued *Statement of Position 95-5—Auditor’s Report on Statutory Financial Statements of Insurance Enterprises* (SOP 95-5) so that an auditor’s opinion on a “prescribed or permitted” basis could continue until codification was completed. SOP 95-5 states “The codification is expected to result in a hierarchy of statutory accounting practices that will provide a comprehensive basis of accounting that can be applied consistently to all insurance enterprises.” At that time, it was believed that once Codification was effective, in order for certified public accountants (CPAs) to issue opinions on statutory statements, SAP had to be considered an “Other Comprehensive Basis of Accounting” (OCBOA) by the American Institute of Certified Public Accountants (AICPA).

19. Codification is not intended to preempt state legislative and regulatory authority. While Codification is expected to be the foundation of a state’s statutory accounting practices, it may be subject to modification by practices prescribed or permitted by a state’s insurance commissioner. Statutory financial statements will continue to be prepared on the basis of accounting practices prescribed or permitted by the states. As a result, in 1998 the AICPA’s Insurance Companies Committee determined that it will not be necessary for the Auditing Standards Board to grant the Codification status as an OCBOA since it will not be the sole basis for preparing statutory financial statements. Further, auditors will be permitted to continue to provide audit opinions on practices prescribed or permitted by the insurance department of the state of domicile.

**F. Scope of Project**

20. The conceptual framework used in developing and maintaining statutory accounting principles for insurance companies is summarized in the Statutory Accounting Principles Statement of Concepts. The application of the concepts of conservatism, consistency and recognition assure that guidance developed and codified as part of this project is consistent with the underlying objectives of statutory accounting.

21. This Guide has been developed using the body of statutory accounting principles as prescribed in the statutory hierarchy of accounting guidance, which is incorporated into the Statement of Concepts. This hierarchy provides the guidance for judging the presentation of statutory financial statements in conformance with statutory accounting principles.

## Preamble

September 20, 1994

## III. Statutory Accounting Principles Statement of Concepts

## Purpose of Statement of Concepts for Statutory Accounting Principles

22. This document states the fundamental concepts on which statutory financial accounting and reporting standards are based. These concepts provide a framework to guide the National Association of Insurance Commissioners ("NAIC") in the continued development and maintenance of statutory accounting principles ("SAP" or "statutory basis") and, as such, these concepts and principles constitute an accounting basis for the preparation and issuance of statutory financial statements by insurance companies in the absence of state statutes and/or regulations.<sup>1</sup>

23. The NAIC and state insurance departments are primarily concerned with statutory accounting principles that differ from GAAP reflective of the varying objectives of regulation. Recodification of areas where SAP and GAAP are parallel is an inefficient use of limited resources.

24. SAP utilizes the framework established by GAAP.<sup>2</sup> This document integrates that framework with objectives exclusive to statutory accounting. The NAIC's guidance on SAP is comprehensive for those principles that differ from GAAP based on the concepts of statutory accounting outlined herein. Those GAAP pronouncements that are not applicable to insurance companies will not be adopted by the NAIC. For those principles that do not differ from GAAP, the NAIC may specifically adopt those GAAP Pronouncements to be included in statutory accounting. GAAP Pronouncements do not become part of SAP until and unless adopted by the NAIC.

25. The body of statutory accounting principles is prescribed in the statutory hierarchy of accounting guidance. This hierarchy provides the framework for judging the presentation of statutory financial statements in conformance with statutory accounting principles.

26. Statutory requirements vary from state to state. While it is desirable to minimize these variations, to the extent that they exist it is the objective of NAIC statutory accounting principles to provide the standard against which the exceptions will be measured and disclosed if material.

## Objectives of Statutory Financial Reporting

27. The primary responsibility of each state insurance department is to regulate insurance companies in accordance with state laws with an emphasis on solvency for the protection of policyholders. The ultimate objective of solvency regulation is to ensure that policyholder, contract holder and other legal obligations are met when they come due and that companies maintain capital and surplus at all times and in such forms as required by statute to provide an adequate margin of safety. The cornerstone of solvency measurement is financial reporting. Therefore, the regulator's ability to effectively determine relative

<sup>1</sup>As stated in the NAIC's constitution, the NAIC is an association of chief insurance regulatory officials of the 50 states, the District of Columbia, American Samoa, Guam, Puerto Rico, and the Virgin Islands whose objective is to serve the public by assisting several state insurance supervisory officials, individually and collectively, in achieving the following fundamental insurance regulatory objectives:

1. Maintenance and improvement of state regulation of insurance in a responsive and efficient manner;
2. Reliability of the insurance institution as to financial solidity and guaranty against loss;
3. Fair, just, and equitable treatment of policyholders and claimants.

<sup>2</sup>The GAAP framework applicable to insurance accounting is set forth in *Statements of Financial Accounting Concepts One, Two, Five, and Six*. These documents, promulgated by the Financial Accounting Standards Board, set forth the objectives and concepts which are used in developing accounting and reporting standards.

#### Preamble

financial condition using financial statements is of paramount importance to the protection of policyholders. An accounting model based on the concepts of conservatism, consistency, and recognition is essential to useful statutory financial reporting.

28. Statutory reporting applies to all insurers authorized to do business in the United States and its territories, and requires sufficient information to meet the statutory objectives. However, statutory reporting as contained in this guide is not intended to preempt state legislative and regulatory authority. The SAP financial statements include the balance sheet and related summary of operations, changes in capital and surplus, and cash flow statements. Because these basic financial statements cannot be expected to provide all of the information necessary to evaluate an entity's short-term and long-term stability, management must supplement the financial statements with sufficient disclosures (e.g., notes to financial statements, management's discussion and analysis, and supplementary schedules and exhibits) to assist financial statement users in evaluating the information provided.

#### Concepts

##### Conservatism

29. Financial reporting by insurance enterprises requires the use of substantial judgments and estimates by management. Such estimates may vary from the actual amounts for numerous reasons. To the extent that factors or events result in adverse variation from management's accounting estimates, the ability to meet policyholder obligations may be lessened. In order to provide a margin of protection for policyholders, the concept of conservatism should be followed when developing estimates as well as establishing accounting principles for statutory reporting.

30. Conservative valuation procedures provide protection to policyholders against adverse fluctuations in financial condition or operating results. Statutory accounting should be reasonably conservative over the span of economic cycles and in recognition of the primary responsibility to regulate for financial solvency. Valuation procedures should, to the extent possible, prevent sharp fluctuations in surplus.

##### Consistency

31. The regulators' need for meaningful, comparable financial information to determine an insurer's financial condition requires consistency in the development and application of statutory accounting principles. Because the marketplace, the economic and business environment, and insurance industry products and practices are constantly changing, regulatory concerns are also changing. An effective statutory accounting model must be responsive to these changes and address emerging accounting issues. Precedent or historically accepted practice alone should not be sufficient justifications for continuing to follow a particular accounting principle or practice which may not coincide with the objectives of regulators.

##### Recognition

32. The principal focus of solvency measurement is determination of financial condition through analysis of the balance sheet. However, protection of the policyholders can only be maintained through continued monitoring of the financial condition of the insurance enterprise. Operating performance is another indicator of an enterprise's ability to maintain itself as a going concern. Accordingly, the income statement is a secondary focus of statutory accounting and should not be diminished in importance to the extent contemplated by a liquidation basis of accounting.

33. The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due

**Preamble**

to encumbrances or other third party interests should not be recognized on the balance sheet but rather should be charged against surplus when acquired or when availability otherwise becomes questionable.

34. Liabilities require recognition as they are incurred. Certain statutorily mandated liabilities may also be required to arrive at conservative estimates of liabilities and probable loss contingencies (e.g., interest maintenance reserves, asset valuation reserves, and others).

35. Revenue should be recognized only as the earnings process of the underlying underwriting or investment business is completed. Accounting treatments which tend to defer expense recognition do not generally represent acceptable SAP treatment.

36. SAP income reflects the extent that changes have occurred in SAP assets and liabilities for current period transactions, except changes in capital resulting from receipts or distributions to owners. SAP income also excludes certain other direct charges to surplus which are not directly attributable to the earnings process (e.g., changes in nonadmitted assets).

**Conclusion**

37. This document states the fundamental concepts for financial statements presented on the basis of SAP. These concepts summarize the conceptual framework that the NAIC uses in developing and maintaining statutory accounting principles for insurance companies. These concepts will also assure that guidance will be provided consistently with the underlying objectives of statutory accounting and will aid in the review of emerging accounting issues.

38. The multitude of unique circumstances and individual transactions makes it virtually impossible for any codification of accounting principles to be totally comprehensive. Application of SAP, either contained in the SSAPs or defined as GAAP and adopted by the NAIC, to unique circumstances or individual transactions should be consistent with the concepts of conservatism, consistency, and recognition.

Exhibit C

**Statement of Statutory Accounting Principles No. 4**

**Assets and Nonadmitted Assets**

**STATUS**

Type of Issue ..... Common Area  
Issued..... Initial Draft  
Effective Date..... January 1, 2001  
Affects ..... Supersedes SSAP No. 87 with guidance incorporated August 2011;  
Nullifies and incorporates INT 01-03  
Affected by ..... No other pronouncements  
Interpreted by ..... INT 01-31  
Relevant Appendix A Guidance..... None

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STATUS ..... 1  
SCOPE OF STATEMENT ..... 3  
SUMMARY CONCLUSION..... 3  
Assets Pledged as Collateral or Otherwise Restricted ..... 4  
Disclosure ..... 4  
Relevant Literature ..... 4  
Effective Date and Transition ..... 4  
REFERENCES ..... 4  
Relevant Issue Papers ..... 4

SSAP No. 4

Statement of Statutory Accounting Principles

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## Assets and Nonadmitted Assets

## SCOPE OF STATEMENT

1. This statement establishes the definition of an "asset" for use in statutory accounting and establishes the criteria for consistent treatment of nonadmitted assets.

## SUMMARY CONCLUSION

2. For purposes of statutory accounting, an asset shall be defined as: probable<sup>1</sup> future economic benefits obtained or controlled by a particular entity as a result of past transactions or events. An asset has three essential characteristics: (a) it embodies a probable future benefit that involves a capacity, singly or in combination with other assets, to contribute directly or indirectly to future net cash inflows, (b) a particular entity can obtain the benefit and control others' access to it<sup>2</sup>, and (c) the transaction or other event giving rise to the entity's right to or control of the benefit has already occurred. These assets shall then be evaluated to determine whether they are admitted. The criteria used is outlined in paragraph 3.

3. As stated in the Statement of Concepts, "The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third-party interests should not be recognized on the balance sheet," and are, therefore, considered nonadmitted. For purposes of statutory accounting principles, a nonadmitted asset shall be defined as an asset meeting the criteria in paragraph 2, which is accorded limited or no value in statutory reporting, and is one which is:

- a. Specifically identified within the *Accounting Practices and Procedures Manual* as a nonadmitted asset; or
- b. Not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*.

If an asset meets one of these criteria, the asset shall be reported as a nonadmitted asset and charged against surplus unless otherwise specifically addressed within the *Accounting Practices and Procedures Manual*. The asset shall be depreciated or amortized against net income as the estimated economic benefit expires. In accordance with the reporting entity's written capitalization policy, amounts less than a predefined threshold of furniture, fixtures, equipment, or supplies, shall be expensed when purchased.

4. Transactions which do not give rise to assets as defined in paragraph 2 shall be charged to operations in the period the transactions occur. Those transactions which result in amounts which may meet the definition of assets, but are specifically identified within the *Accounting Practices and Procedures Manual* as not giving rise to assets (e.g., policy acquisition costs), shall also be charged to operations in the period the transactions occur.

5. The reporting entity shall maintain a capitalization policy containing the predefined thresholds for each asset class to be made available for the department(s) of insurance.

<sup>1</sup> FASB Statement of Financial Accounting Concepts No. 6, *Elements of Financial Statements*, states:

Probable is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in FASB Statement No. 5, *Accounting for Contingencies*, paragraph 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved.

<sup>2</sup> If assets of an insurance entity are pledged or otherwise restricted by the action of a related party, the assets are not under the exclusive control of the insurance entity and are not available to satisfy policyholder obligations due to these encumbrances or other third party interests. Thus, pursuant to paragraph 2(c), such assets shall not be recognized as an admitted asset on the balance sheet. Additional guidance for assets pledged as collateral is included in INT 01-31.

**Assets Pledged as Collateral or Otherwise Restricted**

6. Assets that are pledged to others as collateral or otherwise restricted (not under the exclusive control of the insurer, subject to a put option contract, etc.) shall be identified in the investment schedules pursuant to the codes in the annual statement instructions, disclosed in accordance with *SSAP No. 1—Accounting Policies, Risks & Uncertainties, and Other Disclosures* (SSAP No. 1), reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for assets pledged as collateral or otherwise restricted. Restricted assets should be reviewed to determine admitted or nonadmitted assets status in the statutory financial statements per the terms of their respective SSAPs. Asset restrictions may be a factor in determining the admissibility of an asset under a respective SSAP<sup>3</sup>. However, determining that a restricted asset is an admitted asset does not eliminate the statutory requirements to document and identify the asset as one that is pledged as collateral or otherwise restricted.

7. Assets pledged as collateral are one example of assets that are not under the exclusive control of the insurer, and are therefore restricted, even if the assets are admitted under statutory accounting guidelines (e.g., the asset is substitutable and/or other related SSAP conditions are met). As such, the asset shall be coded as pledged in the investment schedules pursuant to the annual statement instructions, disclosed in accordance with SSAP No. 1, reported in the general interrogatories, and included in any other statutory schedules or disclosure requirements requesting information for assets pledged as collateral or otherwise restricted.

**Disclosure**

8. The financial statements shall disclose if the written capitalization policy and the resultant predefined thresholds changed from the prior period and the reason(s) for such change.

**Relevant Literature**

9. This statement adopts *FASB Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements*, paragraphs 25-33.

**Effective Date and Transition**

10. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with *SSAP No. 3—Accounting Changes and Corrections of Errors*. Guidance reflected in paragraphs 3, 5 and 8, incorporated from SSAP No. 87, was originally effective for years beginning on and after January 1, 2004. The guidance in footnote 2 to paragraph 2 was originally contained within *INT 01-03: Assets Pledged as Collateral or Restricted for the Benefit of a Related Party* and was effective June 11, 2001.

**REFERENCES****Relevant Issue Papers**

- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*
- *Issue Paper No. 119—Capitalization Policy, An Amendment to SSAP Nos. 4, 19, 29, 73, 79 and 82*

<sup>3</sup> An example of such a situation is detailed in footnote 2 pertaining to assets restricted by the action of a related party. This is only a single example and each restricted asset would need to be reviewed to ensure it qualifies as an admitted asset.

Additional  
Supporting  
Documentation

**STATEMENT SUBMITTED BY COLLEEN RIEDEL**

United States Senate Committee On Banking, Housing, and Urban Affairs  
Hearing On: Current Issues in Insurance  
September 08, 2022 10:00 a.m Testimony of Colleen Riedel

Chairman Brown and Ranking Member Toomey and members of the committee, thank you for the opportunity to submit this testimony for the record.

My name is Colleen Riedel. I started with the Northwestern Bell Telephone Company as an Operator in 1964. My first day of orientation at the company was the day after I graduated high school. I would continue to work for the telephone company in Iowa, which became US West and then Qwest, until I retired in December 2000.

I worked my career under union contracts that gave me the opportunity to earn a monthly pension benefit to secure my retirement. The pension benefits that my husband and I continue to receive after more than 20 years have allowed us to maintain a comfortable retirement.

On October 29th of last year I received a notice in the mail that my former employer had purchased a group annuity contract from the Athene Annuity and Life Company, meaning that the company now called Lumen would no longer be responsible for paying my monthly retirement benefits. My benefits would be paid by Athene beginning March 1 of this year.

I recently learned that this announcement from Lumen followed only three months after Lumen's announcement that it had entered a deal to sell operations in 20 states to funds operated by a private equity firm called Apollo Global Management for \$7.5 billion.<sup>1</sup> Apollo Global Management founded Athene Holding Ltd., which is the parent company of the Athene Annuity and Life Company, and on January 3rd of this year the two companies announced a merger to bring the companies together into a new combined operation.<sup>2</sup> I find it concerning that the arrangement to administer and secure my retirement benefits has the appearance of being connected to an unrelated transaction between the same companies.

Although the notice from Lumen assured me that my pension benefit would not change, I have since learned that is not the case. I found that upon moving to Athene, there were significant disruptions in the administration of my benefit, in particular involving incorrect tax and benefit deductions. In addition, my pension benefit used to be guaranteed by the Pension Benefit Guaranty Corporation when it was administered by Lumen. Because I live in the state of Iowa, the Iowa Life & Health Insurance Guaranty Association now has responsibility for ensuring the payment of my benefits. I worked my

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<sup>1</sup> <https://news.lumen.com/2021-08-03-lumen-to-sell-local-incumbent-carrier-operations-in-20-states-to-apollo-funds-for-7-5-billion>

<sup>2</sup> <https://www.athene.com/our-story>, <https://www.apollo.com/media/press-releases/2022/01-03-2022-120051006>

career under the assurance that my earned pension benefit would have the protections of PBGC insurance and found this to be a significant change.

This issue of a government backstop is especially concerning to me because private equity companies like Apollo Global Management have a track record of prioritizing short-term profits at the expenses of workers and retirees. I have been glad to see that Chairman Brown has been a leader on this issue and has pushed for greater transparency and analysis of the increasing role that private equity companies are playing in the administration of life insurance and annuity benefits.

I thank the Chairman and the Committee for providing me the opportunity to share my experiences on this issue.

**LETTER SUBMITTED BY THOMAS F. GOODWIN, VICE PRESIDENT,  
EXHIBITIONS AND CONFERENCES ALLIANCE**



September 8, 2022

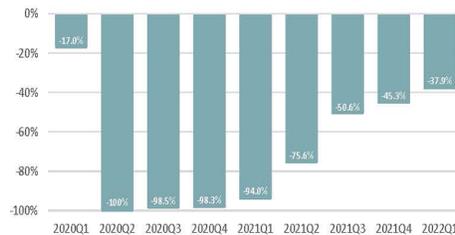
The Honorable Sherrod Brown  
The Honorable Pat Toomey  
U.S. Senate Committee on Banking, Housing and Urban Affairs  
534 Dirksen Senate Office Building  
Washington, DC 20510

Dear Chairman Brown and Ranking Member Toomey:

On behalf of the Exhibitions & Conferences Alliance (ECA), thank you for hosting today's Committee hearing on *Current Issues in Insurance*. As our nation continues to emerge from the devastating economic impacts of COVID-19, one of the most pressing insurance issues today is the development of a new insurance program that protects American jobs by ensuring businesses continuity from economic losses caused by future pandemics.

ECA is an alliance of nine associations dedicated to the recovery and advancement of the face-to-face business events industry. Prior to the pandemic, our industry contributed \$396 billion annually to U.S. gross domestic product and supported 6.6 million jobs nationwide. Importantly, small businesses are the driving force behind face-to-face business events—which includes conventions, trade shows, expositions, and large conferences—with 99% of our industry's companies meeting the U.S. Small Business Administration's size standards for small businesses. In addition, face-to-face business events are growth engines for so many other small businesses across every major sector of the U.S. economy. Of the 1.7 million exhibitors at face-to-face business events in 2019, more than 80% were small businesses themselves.

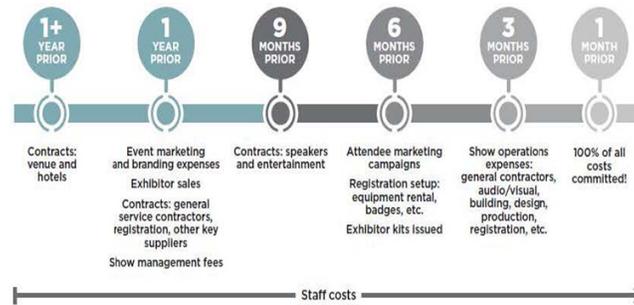
Unfortunately, our industry is still recovering from the economic devastation of the pandemic. The Center for Exhibition Industry Research recently reported that the business-to-business events sector was still down 37.9% from pre-pandemic levels in the first quarter of 2022, with similar levels of negative impact in other parts of the industry.



Center for Exhibition Industry Research • Destinations International • Experiential Designers & Producers Association  
Exhibition Services & Contractors Association • International Association of Exhibitions and Events  
International Association of Venue Managers • Society of Independent Show Organizers • Trade Show Labor Alliance • UFI

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One critical factor slowing the return of face-to-face business events is the inability for event organizers within the industry to obtain communicable disease coverage for future pandemics as part of their event cancellation insurance. As you can see below, significant expenses for business events begin accruing one year or more in advance of the actual event taking place.



Given the front-loaded nature of these expenses, many convention and trade show organizers, including smaller organizers and those affiliated with associations and other non-profit organizations, are financially unable to take on the overwhelming risk of putting on uninsurable face-to-face business events. This collapse within the insurance marketplace is significantly limiting our industry's ability to bring back events, which are critical to accelerating rehiring. This impedes both our industry's recovery and our ability to support the many small businesses in Ohio, Pennsylvania, and nationwide who rely on our events to nurture, cultivate, and grow their businesses.

Here is an illustrative case study: Exposition Development Company, Inc. (ExpoDevCo) is a boutique trade show company with 17 employees that organizes 11 events across the country. In 2020, its restaurant industry trade show was cancelled due to COVID-19. ExpoDevCo had to refund more than \$1 million in exhibit space. In addition, there were \$675,000 in unrecoverable expenses associated with the event. The company's event cancellation insurance, which included communicable disease coverage, paid out nearly \$800,000, which allowed the company to continue operations and retain all of its employees. If that happened today, however, without communicable disease coverage, ExpoDevCo would be forced to close its doors permanently.

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That's why ECA supports bipartisan efforts in the Senate to help restore communicable disease coverage as part of event cancellation insurance. By establishing a public-private backstop that ensures that our industry, and the U.S. economy more broadly, is properly protected against pandemic-related risk going forward, both for-profit and non-profit event organizers alike will benefit from the restoration of a thriving private-sector event cancellation insurance marketplace that offers them the policies they need to bring back face-to-face events at scale without putting the future of their respective organizations at risk.

In closing, as the face-to-face business events industry continues to get back to business nationwide, a new pandemic risk insurance program will help us bring back jobs, accelerate our industry's recovery, and support countless small businesses and non-profit organizations in the months and years to come.

ECA stands ready to support the work of the Committee as it works constructively to address future pandemic risk. If you or your staff have any questions, or if ECA can provide additional information on this important issue, please do not hesitate to contact me at (703) 539-5875 or via email at [tommy.goodwin@ecalliance.us](mailto:tommy.goodwin@ecalliance.us). Thank you.

Sincerely,

A handwritten signature in black ink, appearing to read 'Tommy', with a horizontal line extending to the right.

Thomas F. (Tommy) Goodwin  
Vice President

**LETTER SUBMITTED BY MARY KATE CUNNINGHAM, SENIOR VICE PRESIDENT, PUBLIC POLICY, AMERICAN SOCIETY OF ASSOCIATION EXECUTIVES**



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[asaecenter.org](http://asaecenter.org)

September 8, 2022

**The Honorable Sherrod Brown**  
**The Honorable Pat Toomey**  
U.S. Senate Committee on Banking, Housing and Urban Affairs  
534 Dirksen Senate Office Building  
Washington, D.C. 20510

**RE: ASAE Written Statement for September 8, 2022 Current Issues in Insurance Hearing. Establishing Pandemic Risk Insurance is Essential to Support Workers and Employers.**

Dear Chairman Brown and Ranking Member Toomey:

Thank you for examining current issues in insurance during your committee-wide hearing on September 8, 2022. The American Society of Association Executives (ASAE), which represents thousands of trade and professional associations and is a proud member of the Business Continuity Coalition, urges Congress to establish a public-private pandemic risk insurance program.

Associations, event venues, hospitality providers and the millions of companies and employees they support need pandemic risk insurance to protect jobs and our community's far-reaching economic impact. Associations promote all industries and professions through myriad revenue-generating events, such as conventions, trade shows and business meetings.

Communicable disease coverage for event cancellation was available in February 2020 but is virtually nonexistent today. As a result, associations and other employers have no recourse but to face untenable risk should another pandemic strike.

Associations dedicate an average of 35 percent of their budgets to meetings and events.<sup>1</sup> This commitment supports all 15.7 million Americans who work in the hospitality industry,<sup>2</sup> which was devastated by the pandemic.

**According to ASAE Research Foundation surveys and data reports:**

- 15% of associations conduct at least 50 revenue-generating events per year.
- Approximately 0% of organizations that possessed communicable disease coverage for cancelled events before the pandemic can access the same coverage today.
- 70% of surveyed organizations report higher premiums and less coverage.
- Premiums have increased an average of 35% since the pandemic (and with less coverage).
- 60% report using financial reserves to cover losses from cancelled events.
- 13% report insufficient financial reserves to cover losses from cancelled events.
- 92% are concerned about hosting future revenue-generating events.

<sup>1</sup> Professional Convention Management Association. 26th Annual Meetings Markey Survey.

<sup>2</sup> Bureau of Labor Statistics. <https://www.bls.gov/lag/tots/lag70.htm>.

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Among 230 surveyed organizations, 550 revenue-generating events were cancelled in 2021, resulting in a loss of \$165 million. These losses account for host organizations only and not for evaporated benefit to local economies. ASAE's Annual Meeting, for example, injects roughly \$16 million into local economies over five days. Its 2018 event produced an additional \$147 million in downstream economic impact within one year.<sup>3</sup>

**Major events are paramount for associations, workers, industries and professions because they:**

- Generate funds that organizations rely on to pay staff, support essential services and pursue their missions in public service;
- Facilitate innovation, training, education, and knowledge-sharing to build up businesses and employees that span the economy (particularly amid challenging circumstances);
- Provide for regional, state and federal tax revenues; and
- Collectively generate massive local economic impact (e.g., hotel stays, venue contracts, dining, entertainment, etc.).

Thank you for your service to our country and thoughtful consideration of current issues in insurance. Please contact me at [mcunningham@asaecenter.org](mailto:mcunningham@asaecenter.org) or 202-626-2787 if you have questions or would like more information.

Sincerely,



Mary Kate Cunningham, CAE  
Senior Vice President, Public Policy  
American Society of Association Executives

CC:

Members of the U.S. Senate Committee on Banking, Housing and Urban Affairs

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<sup>3</sup> Choose Chicago (Chicago, Illinois Convention & Visitors Bureau) Economic Reporting.