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## State regulators clash with insurers on Capitol Hill

### Insurance group argue that federal regulation is needed for systemic risk

By [Ronald D. Orol](#), MarketWatch

Last update: 11:30 a.m. EDT March 17, 2009

**WASHINGTON (MarketWatch) - State regulators and insurance companies clashed on Tuesday over whether lawmakers should create an optional federal charter for the fragmented U.S. insurance industry.**

Michael McRaith, director at the National Association of Insurance Regulators, told lawmakers in the Senate Banking Committee that an optional federal charter would lead to a system where the insurer chooses the regulator with the "lightest touch." McRaith argued that an ability to choose between a state and federal regulator would lead to regulatory arbitrage and failures.

U.S. insurance companies, including troubled American International Group Inc. ([AIG](#)), must now comply with 51 sets of different regulations, one for each state.

An optional federal charter would allow larger insurance companies to choose between the existing state system and a new national regulatory structure that would eliminate the need to comply with the different state regulators.

With a federal charter, not all insurance companies could qualify to participate as national insurance companies. Congress would need to decide whether only insurance companies of a certain size, based on assets under management or the volume of policies they provide, would be permitted to be a federally chartered insurance company.

Supporting the federal charter idea, Frank Keating, president of the American Council of Life Insurers, told lawmakers that a federal regulator with an optional federal charter is necessary so G-20 countries can coordinate on systemic risk issues. Setting up an optional federal charter could also help to eliminate a competitive disadvantage for U.S. insurers in a global economy, where rival global insurers typically operate under a federal regulator in their home jurisdiction, he added.

"Absent a federal regulator with an in-depth understanding of the industry, how can vital information on the insurance industry can be effectively collected and analyzed?," Keating asked.

Key lawmakers did not indicate that they opposed or supported a federal charter. Senate Banking Committee Chairman Christopher Dodd, D-Conn., said state regulation has been a source of innovation and consumer protection. However, he added the insurance industry has become complex and international in recent years, which may require a "modernization" of the system.

Dodd indicated he was supportive of, at the very least, setting up an office of insurance information in the federal government. "There is a lack of expertise on insurance in the federal level," Dodd said. "There is no central depository of information about the insurance industry."

All seven insurance officials testifying at the committee said they supported the creation of such an information depository.

Sen. Richard Shelby, ranking member of the committee, indicated he was more supportive of an optional federal charter. "If insurers are managing risks on a national basis, it may make sense to consider regulating them on a national basis," Shelby said.

### Dealing with systemic risks

Both Dodd and Shelby added that the near-collapse of AIG, which has received \$173 billion in government-funded bank bailout funds, raises the question of whether the U.S. needs a federal systemic risk regulator. Such a regulator, could be housed in the Federal Reserve System, and would be responsible for identifying and regulating financial institutions that they deem to be too big to fail.

Dodd said he thought that perhaps some insurance products raise systemic risks, such as problematic credit default swaps, which act as mortgage securities insurance, and may need to be considered by a systemic risk regulator.

Proponents of a new chartering system argue that AIG and other insurance companies are being treated from the perspective of systemic risk as equivalent to many federally chartered banks, however the insurer is regulated on a state-by-state basis.

However, Spencer Houldin, director at the Independent Insurance Agents & Brokers of America, said state regulation continues to protect consumers, making an optional federal charter unnecessary. He raised concerns about creating an optional federal charter because of problems with AIG, which he argued is a unique business entity.

"Does anyone really think that allowing AIG to pick its regulator would fix its options?" Houldin asked.

### AIG bonus problem

Dodd also said on Tuesday said he wants a briefing from the Federal Reserve System on \$163 billion in bonuses that were paid out by AIG.

"We want and expect a full briefing," said Dodd. "And we also want answers regarding where the Fed has been on conditions for these types of bonuses since the rescue effort first began."

Dodd said he will work on a plan to get the bonus money back.

Dodd added that he is ready to help the Obama administration in this effort. President Barack Obama on Monday said he will seek to block AIG's bonus payments, however financial experts argue that executive compensation contracts are binding and cannot be broken up. However, the Obama administration may seek to use a \$30 billion piece of AIG's bank bailout package approved on March 2 as leverage. The government will seek to have AIG adjust its bonus packages to make sure that no government funds will be used to pay bonuses.

Other lawmakers also said they were outraged by the AIG bonuses.

"What do taxpayers get for throwing \$173 billion, they get \$163 million in bonuses," said Sen. Jon Tester, D-Mont., "This is incredibly unacceptable. It makes sense to me that they should go broke. The only reason that they even have a job is because of taxpayers funding. This is ridiculous."

Shelby said he wanted to have the bank bailout inspector general to testify before the committee to examine the use of government funds as part of a \$700 billion bank bailout funds. ■

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