STATEMENT

OF

THE AMERICAN COUNCIL OF LIFE INSURERS

BEFORE THE

HOUSE COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON HOUSING & INSURANCE

ON

"THE IMPACT OF INTERNATIONAL REGULATORY STANDARDS
ON THE COMPETITIVENESS OF U.S. INSURERS: PART II"

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STATEMENT MADE BY

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Chairman Luetkemeyer, Ranking Member Cleaver, and members of the Committee, I am pleased to present this statement expressing the views of the American Council of Life Insurers (ACLI) regarding international insurance standards. The ACLI is a Washington, D.C.-based trade association with approximately 300 member companies operating in the United States and abroad. ACLI advocates in federal, state, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing more than 90 percent of industry assets and premiums.

LIFE INSURERS ARE ESSENTIAL TO RETIREMENT SECURITY

In the United States and around the world, retirement security is an increasingly urgent problem. Populations are aging, the ratio of workers to retirees is declining, and governments are struggling to support the avalanche of retirees joining public retirement systems. Traditional pension plans that provide lifetime income are increasingly unavailable. Whether or not public programs will be able to continue to provide retirement benefits at current levels is an open question, and one that has dramatic consequences for the quality of life for millions of families. Financial security for families and dignity for all in retirement should be a goal of governments around the world.

The life insurance industry is uniquely suited to provide retirement solutions. Life insurers provide risk protection, insurance, and annuities products that help families save for retirement and ensure guaranteed income for life. Annuities are the sole means available in the marketplace today by which retirees can secure income for life. Now more than ever, life insurance companies are essential to helping families build and achieve retirement security. By strengthening retirement security, life insurers are improving the lives of retirees and also reducing demands on public programs.

LIFE INSURERS SUPPORT THE ECONOMY THROUGH LONG-TERM INVESTMENT

Life insurers are also important contributors to economic growth as long-term investors. Life insurers are leading purchasers of corporate bonds, which fund business expansion, innovation, job growth, and infrastructure. Because life insurers make guarantees that often last many decades, they must invest in assets that have the same long-term horizon. This kind of asset-liability duration matching is not only a fundamental principle of prudential regulation of insurers, but also positions life insurers to be a powerful source of long-term capital and economic growth. The bonds that life insurers purchase today have an average maturity of more than 18 years.

INTERNATIONAL CAPITAL STANDARDS SHOULD NOT PRECEDE DOMESTIC CAPITAL STANDARDS

Both the Federal Reserve Board (Board) and the International Association of Insurance Supervisors (IAIS) are developing insurance capital standards that are likely to have significant impacts on life insurance companies and the families who depend on them for financial and retirement security. If these standards are bank-centric or inconsistent, they will disrupt the marketplace and undermine the ability of life insurers to provide long term, guaranteed retirement products to savers and retirees. To ensure the best possible outcome for policyholders, the Board should utilize the flexibility provided in the Insurance Capital Standards Clarification Act, develop an insurance capital standard that is appropriate for U.S. insurers and the insurance business model, and partner with the other U.S. representatives to the IAIS (Treasury's Federal Insurance Office (FIO) and state insurance supervisors) to ensure that any international insurance standards reflect the unique strengths of the U.S. system of insurance supervision. As I will describe more fully later, U.S. insurance products are currently treated unfairly by the IAIS, which has approved a higher capital charge for U.S. variable annuity products but not for products offered in other countries with similar risk characteristics. U.S. insurance products must not be placed at a competitive disadvantage by international capital standards and all insurance products with similar risk characteristics should be treated equally regardless of their national jurisdictions.

The ACLI thanks Chairman Luetkemeyer, Ranking Member Cleaver, and the members of this committee for their support of the Insurance Capital Standards Clarification Act in the last Congress. As a result of the bipartisan leadership of this committee, as well as bill authors Representative Gary Miller, Representative Carolyn McCarthy, Senator Susan Collins, Senator Sherrod Brown, and Senator Mike Johanns, both the House and Senate passed the Insurance Capital Standards Clarification Act by a unanimous vote, providing a clear statement that Congress supports appropriate capital standards for insurance companies. ACLI strongly supports utilization of the flexibility provided in that law and urges continued congressional oversight to ensure that the intent of Congress and the competitiveness of the U.S. insurance industry is preserved. ACLI commends the Board for its plan to conduct formal rulemaking with notice and public comment, and for its many public statements, including in testimony before this Committee, that it intends to exercise the discretion authorized by Congress to tailor capital standards to insurance companies. The Board's plan to tailor standards is very appropriate and will further the interests of prudential supervision of insurance companies.

It is essential that policymakers correctly address insurance capital standards here in the U.S. first, so that our Team U.S.A. representatives to the IAIS have a stronger, unified position in any international discussions. Common sense suggests that the U.S. should conduct its own process for the development of an insurance capital standard before agreeing to any international standards. The ACLI believes that it is in the best interests of the U.S. to focus on the domestic rulemaking first and ensure that the domestic process is as thoughtful, informed, and transparent as possible.

Any insurance capital standard must reflect the long-term nature of life insurers' investments and the need to match investments with the long-term duration of insurance liabilities. Bank standards that favor short-term assets simply do not work for the insurance company business model, in which commitments to insurance policyholders and annuity investors often last many decades. The ACLI believes that any consolidated capital standards developed by the Board for insurance companies should be modeled on the state insurance risk-based capital system. State risk-based capital standards are comprehensive standards specifically designed by insurance regulators to measure the unique risks of the insurance company business model.

U.S. LEADERSHIP AT FSB AND IAIS PROTECTS U.S. COMPETITIVENESS

The influence of the Financial Stability Board (FSB) and the development of capital standards by the IAIS, including the insurance capital standard (ICS) and Higher Loss Absorbency (HLA) requirements, represent a significant change in the development of standards for the insurance industry. The development of international insurance capital standards means that U.S. federal agency leadership by the Treasury Department and Federal Reserve Board, in partnership with state insurance regulators, is more important than ever before. The full involvement of Treasury and the Board in FSB and IAIS activities is absolutely essential to influencing the international process and ensuring that international standards reflect the unique strengths of the U.S. system for prudential insurance regulation.

Team U.S.A. representatives should work to ensure that any global capital standards do not disadvantage U.S. insurers and the families that rely on them for financial security. Any restriction on the ability of Team U.S.A. to participate in international standard setting organizations would in no way protect the U.S. insurance industry and U.S. insurance consumers.

COOPERATION AND COORDINATION OF TEAM U.S.A. APPROACH IS ESSENTIAL

ACLI commends the three U.S. insurance representatives to the IAIS (the Board, FIO, and state insurance supervisors) for the important partnership that they have established in the Team U.S.A. approach. Team U.S.A. will be best positioned to represent the U.S. and secure the best outcome for U.S. consumers and insurers only by working together, meeting regularly, coordinating their efforts, and agreeing to common objectives. The Team U.S.A. concept constitutes a cooperative effort to speak with a strong, unified voice as part of any IAIS discussions and ACLI fully agrees with the wisdom of this approach.

FSB AND IAIS PROCESS SHOULD REFLECT GREATER TRANSPARENCY AND ACCOUNTABILITY

The ACLI believes that both the FSB and the IAIS should work to improve their engagement with stakeholders and ensure that their governance procedures meet high standards. Ongoing engagement with stakeholders and transparent processes are critical to the development of thoughtful, informed policies. In the absence of meaningful participation from public stakeholders, policymakers are denied access to a full exchange of ideas and a diversity of perspectives. In contrast, highly transparent processes and greater opportunities for stakeholder participation introduce more information, expertise, and experience to the discussion and increase public confidence in institutions.

IAIS bylaws and the IAIS Policy for Consultation of Stakeholders recognize the critical importance of open and transparent processes. ACLI appreciates this official commitment to transparency and accountability and urges the IAIS to redouble its efforts to make good on this promise. Due to the importance of the work being done by the IAIS, more stakeholder input is necessary, not less. With that in mind, we believe that the IAIS should take the following steps:

- Refrain from developing regulatory standards in isolation from the industry and the markets they serve.
- IAIS consultations should include a comment period of no less than 90 days to allow for thorough review and thoughtful comprehensive responses. For significant standards, 60 days is very often inadequate.
- To achieve the IAIS' stated goal of transparency, IAIS committee, task force and working group rosters must be posted to the IAIS Web site and updated regularly to reflect changes.
- IAIS meeting materials should be made available publicly and stakeholders should have access to agendas, presentations, detailed minutes, and advanced drafts of supervisory material.

COMMENTS ON G-SII ASSESSMENT METHODOLOGY

On January 25, 2016, ACLI provided comments to the IAIS in response to its public consultation on a proposed updated Assessment Methodology for Global Systemically Important Insurers (G-SIIs). ACLI welcomes the IAIS commitment to review and update the Methodology, which must be improved in significant ways. In order to meet the IAIS' goal of reducing systemic risk, the Methodology should focus on the creation and transmission of systemic risk. If not developed properly and fairly, the Methodology may diminish the availability of retirement security products at the expense of aging populations around the world.

We remain concerned that while the IAIS stated its intention to assess on a loss-given-default basis, the Methodology combines criteria that measure impact in the event of default with those that measure the vulnerability to market stress as measures of systemic risk. It also fails to recognize product and risk management techniques that reduce systemic exposures. In addition, the Methodology relies on a relative ranking of insurance firms to determine G-SII status. It is critical that assessment for potential systemic exposure be conducted through a loss-given-default lens and that vulnerabilities be demonstrated to link to a systemic risk transmission channel. It is equally critical that the assessment process be conducted in a transparent manner and include meaningful dialogue with the firm under consideration throughout the process so they understand the basis for their consideration and/or designation and measures that can be pursued to avoid or shed designation.

We would also underscore that there remains little empirical research and data to form the basis for an understanding of how activities insurers engage in could, in the event of disorderly failure, cause significant disruption to the global financial system and economic activity. We believe the IAIS and FSB should consider this threshold question and devote time and resources to improve this understanding.

COMMENTS ON APPROACH TO NON-TRADITIONAL NON-INSURANCE

On January 25, 2016 ACLI provided comments to the IAIS in response to its public consultation on Non-traditional Non-insurance (NTNI) Activities and Products. ACLI is very concerned that the IAIS approach to NTNI is misguided and troubled by the fact that it disproportionately harms guaranteed lifetime income products commonly available in the U.S. Specifically, variable annuities should not be considered NTNI and subject to higher capital charges. These products are strictly regulated by federal and state authorities and have helped consumers in America for 60 years. ACLI strongly believes that the NTNI approach must be fixed. That revision should better recognize the true nature of risk from an insurance balance sheet perspective and must result in a level playing field, particularly with products offered in other countries with similar risk characteristics.

Furthermore, ACLI believes that the IAIS consultation plainly misses its primary objective of considering systemic, macroprudential concerns. The NTNI approach emphasizes analysis of a company's probability of failure, which is a microprudential concern, rather than analysis of how a company's failure might or might not impact the rest of the financial system, which is a macroprudential concern. ACLI supports reorienting the NTNI toward analysis of systemic factors.

ACLI is also concerned that the current NTNI definition excludes balance sheet risk management. The life insurance business model is to assume long-term risks and to implement proven strategies to manage those risks. Any framework that does not acknowledge and account for this critical element is incomplete and would be more likely to yield misleading results.

COMMENTS ON THE DISCUSSION DRAFT

ACLI would like to commend Chairman Luetkemeyer and other members of the Committee for their development of the Discussion Draft on international insurance standards. The Discussion Draft reflects many of the principles of transparency, accountability, and due process that are supported by ACLI and its member companies. The Discussion Draft improves Congressional oversight over international standard setting initiatives for insurance and expresses clear objectives for those initiatives, including maintaining the ability of the U.S. insurance industry to offer the products that U.S. consumers rely upon as part of their financial planning. These important goals are shared by ACLI and underscore the need for transparency and governance reforms at the IAIS and FSB.

ACLI would suggest some further refinements to the Discussion Draft for the consideration of this committee that are consistent with the view that any restriction on the ability of Team U.S.A. to participate fully at international standard setting organizations would be harmful to U.S. interests.

We also have some concerns with the provisions of the Discussion Draft addressing covered agreements, which are not designed for enacting new international capital standards. Rather, they are a mechanism for removing commercial and regulatory barriers that may deny U.S. insurers full and fair access to particular foreign markets and for providing similar fair treatment to foreign insurers seeking access to the United States.

We appreciate that the 30-day public comment period proposed in the draft would run concurrently with the existing Congressional submission and layover requirement in the Dodd-Frank Act. However, we are concerned that the new requirements in the Discussion Draft could interfere with the effectiveness of covered agreements, including the currently pending covered agreement with the European Union, notice of which was published in the Federal Register last month. We pledge to work with the committee to address concerns while also preserving the effectiveness of this very important tool for helping U.S. companies receive fair treatment.

ACLI thanks the Committee for their leadership on this important legislation and looks forward to working with the Committee on suggested changes going forward.

CONCLUSION

Mr. Chairman, thank you for holding this hearing today to highlight the many concerns about international insurance standards. Any standards developed at international organizations must be consistent with the U.S. system for insurance supervision, must not disproportionately harm U.S. products approved and regulated by state insurance supervisors such as variable annuities, and must not interfere with the Board's rulemaking process, including notice and public comment, for development of insurance capital standards for insurers subject to Board supervision. Thank you for the opportunity to testify today and for your consideration of the views of ACLI and its member companies.