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House Committee on Financial Services
Subcommittee on Housing and Insurance
"The Impact of Domestic Regulatory Standards on the U.S. Insurance Market"
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Chairman Luetkemeyer, Ranking Member Cleaver, Members of the Subcommittee, thank you for inviting me to testify today on "The Impact of Domestic Regulatory Standards on the U.S. Insurance Market."

While previous hearings have focused on the international leadership role of the Federal Insurance Office (FIO), FIO also has an important role in domestic insurance matters. FIO monitors all aspects of the insurance industry, including identifying issues or gaps in the regulation of insurers that could contribute to a systemic crisis in the insurance industry or the United States financial system; monitoring 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; recommending to the Financial Stability Oversight Council (FSOC) that it designate an insurer, including the affiliates of such insurer, as an entity subject to regulation as a nonbank financial company supervised by the Board of Governors of the Federal Reserve (Federal Reserve); assisting the Secretary in administering the Terrorism Risk Insurance Program (TRIP) established in Treasury under the Terrorism Risk Insurance Act of 2002, as amended (TRIA); and consulting with the states (including state insurance regulators) regarding insurance matters of national importance and prudential insurance matters of international importance.

Also, before the Secretary may determine whether to seek the appointment of the Federal Deposit Insurance Corporation (FDIC) as receiver of an insurer under Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Secretary must first receive a written recommendation from the FIO Director and the Federal Reserve. Additionally, FIO and the Federal Reserve are authorized to coordinate annual analyses of nonbank financial companies supervised by the Federal Reserve to evaluate whether such companies have the capital, on a consolidated basis, necessary to absorb losses as a result of adverse economic conditions.

The FIO Director is a non-voting member of the FSOC, and FIO participates directly in the FSOC analysis of broader systemic risks and individual firms. In this work, FIO works closely with staff from other FSOC member agencies, including state regulators and staff of the National Association of Insurance Commissioners.

On September 28, FIO published its 2015 annual report on the state of the insurance industry and related developments. As in the past, FIO's 2015 Annual Report includes sections describing (1) a financial overview of the U.S. insurance industry, (2) developments and issues with respect to consumer protection and access to insurance, (3) U.S. regulatory developments, and (4) international regulatory developments. FIO's 2015 Annual Report also addresses the status of recommendations on how to modernize and improve the system of insurance regulation in the United States, as described in FIO's December 2013 report of the same title.

Any discussion of the U.S. insurance sector and its regulation must begin with the recognition that the United States has the most diverse and competitive insurance market in the world. Thousands of insurers operate in the United States, ranging from small mutual companies operating in a few rural counties to massive global firms engaged in a variety of financial activities. While serving as the Illinois Director of Insurance, I learned firsthand about the importance of small and mid-size insurers to the marketplace and to local and regional economies. Consolidation pressures in the small insurer market segment have existed for years, but we recognize and want to preserve the important contributions of local and regional insurers to consumers and communities.

For 2014, insurers operating in the United States continued to report good financial performance and sound financial condition. In combination, total direct premiums for the life and health (L/H) sector and the property and casualty (P/C) sector were a record aggregate high of $1.23 trillion, an amount equaling 7 percent of the U.S. Gross Domestic Product, a welcome increase following a modest decline in total volume from 2012 to 2013.

In total, the insurance industry reported in 2014 $8.3 trillion in assets, with the L/H sector holding approximately $6.3 trillion, the Health sector holding $248 billion, and the P/C sector holding approximately $1.8 trillion.

Taking into account retained earnings, the sector again reached new, record-high levels of capital and surplus. The L/H sector reported $354 billion in capital and surplus, the P/C sector reported approximately $689 billion in capital and surplus, and the Health sector reported $112 billion in capital and surplus.

Due to lower underwriting gains and large intra-group losses, net income decreased in 2014 as compared to 2013. Investment yield continued to suffer from the current low interest rate environment, but net investment income nevertheless showed a small increase on a higher base of invested assets. To partially mitigate declining investment yields, both L/H and P/C insurers have increased asset allocations towards lower rated and less liquid assets with longer durations, an indication of increased portfolio risks. For both the L/H and P/C sectors, growth in expenses, however, outpaced the increase in total revenues, leading to a decline in operating income as compared to 2013. Accordingly, while the insurance industry in aggregate was profitable, net income and return on average equity were below 2013 levels.

Net written premiums are a principal measure of size and growth in the insurance industry. Net written premiums for the L/H sector totaled $648 billion in 2014, marking a 15 percent increase over 2013. Premiums accounted for 74 percent of total L/H sector revenues in 2014, a mark slightly higher than the historical average of 72 percent. This number also corresponds with the smaller amount of risk ceded to third-party reinsurers in 2014. Notably, solid growth in the sector was driven by a 26 percent gain in annuity premiums and deposits, which also represented the majority of total written premiums for the L/H sector.

For the P/C sector, total net written premiums reached another record level of $503 billion, marking more than a 4 percent increase over 2013, supported by more than 5 percent growth in personal lines.

The combined ratio is an accepted insurance sector metric that compares underwriting performance in the P/C sector, with a ratio of less than 100 percent an indication that premiums covered losses and expenses for the year. In 2014, the P/C sector combined ratio was approximately 97 percent, below 100 percent for the second consecutive year.

Although 2014 included more typical loss results than 2013, the P/C sector was helped by a modestly lower expense ratio. 2014 also reversed a declining trend in the P/C net investment income, with a total of $55 billion, or nearly 12 percent improvement over 2013.

In the aggregate, despite concerns regarding a low interest rate environment, the insurance industry reports financial strength in insurance-related activities, in part due to increased consumer demand during this extended period of economic recovery and job growth.

Measuring global market share by aggregate premium volume, the United States' share of the world market declined from 27.5 percent in 2013 to 26.8 percent in 2014. This development reflects both the continued vibrancy of the U.S. market – far and away the world's largest – and the growth opportunities for U.S.-based insurers in developing economies.

FIO continues to move forward with implementation of the Terrorism Risk Insurance Program Reauthorization Act of 2015 (Reauthorization Act). In light of the amendments to TRIP enacted in the Reauthorization Act, FIO issued interim guidance on February 4, 2015, and has engaged extensively with stakeholders in anticipation of revisions to TRIP regulations. FIO has convened stakeholders, including consumers, industry, state regulators, and data aggregators, for the purpose of sorting through important and novel data collection requirements. In addition, through a Notice in the Federal Register published on April 20, 2015, FIO requested candidates to serve on the Advisory Committee on Risk-Sharing Mechanisms that the Reauthorization Act required Treasury to establish. After reviewing applications and selecting applicants to serve on the Advisory Committee on Risk-Sharing Mechanisms, Treasury announced the members of this important committee on September 23, 2015.

Among its authorities, FIO is authorized to monitor 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. For this purpose, FIO has focused initially on the affordability and accessibility of personal auto insurance. FIO selected this line of insurance because personal autos are frequently necessary for consumers to commute to and from work, and for many consumers to tend to their daily family needs, like driving students to and from school. On April 10, 2014, FIO published a Notice in the Federal Register seeking comment on how to define affordability for purposes of this monitoring work. After consideration of the comments received, and extensive analysis and engagement with stakeholders, FIO published in the Federal Register a second Notice, on July 2, 2015, seeking comments on a proposed definition of affordability. The comment period closed on August 31, 2015. Twelve comments were received, all of which are being carefully reviewed and considered. Once complete, our hope is to establish a public definition of affordability in order to facilitate greater dialogue on steps that the sector can take to increase access and affordability of personal lines products. Further, with the development of the definition, FIO will work with stakeholders to develop the tools to monitor affordability and accessibility.

In December 2014, FIO released its report on the breadth and scope of the global reinsurance market and the critical role it plays in supporting insurance in the United States. Despite the continuing development of alternative risk transfer mechanisms in the insurance sector, much of the U.S. primary insurance activity is supported by the global reinsurance industry – a market with many important participants based outside the United States. In fact, based on gross premiums ceded, more than 90 percent of the unaffiliated reinsurance of U.S. property and casualty insurers is placed with a non-U.S. reinsurer or a U.S. reinsurer with a non-U.S. holding company parent.

Regarding other work of interest to this Committee, FIO continues to work collaboratively with the state insurance regulators and the Federal Reserve on matters before the International Association of Insurance Supervisors (IAIS). FIO also continues to reach out to stakeholders, providing appropriate and meaningful opportunities to engage in efforts at the IAIS.

Additionally, FIO and the United States Trade Representative (USTR) continue work to develop a process to negotiate a covered agreement. The pursuit of a covered agreement, which relates only to certain prudential insurance or reinsurance matters, is an authority granted by Congress jointly to Treasury and USTR. We will consult with this and other Committees before negotiations commence. FIO and USTR look forward to meaningful engagement with Congress, state regulators, and other stakeholders throughout the covered agreement process. Importantly, our objective in the negotiation of a covered agreement would be to provide tangible benefits for the U.S. insurance industry and consumers.

In all of our work, Treasury priorities will remain the best interests of U.S. consumers, U.S. insurers, the U.S. economy, and jobs for the American people. We welcome the chance to work with this Committee and its excellent staff, and look forward to more discussions on these and other important topics. Thank you for your attention. I look forward to your questions.