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Mark Carney, Chairman
Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel, Switzerland

Re: Consultative Document: Cross-Border Recognition of Resolution Action

Dear Chairman Carney:

The American Insurance Association ("AIA") welcomes the opportunity to comment on the Financial Stability Board's ("FSB") Consultative Document: Cross-Border Recognition of Resolution Action.

AIA represents approximately 300 major United States insurance companies that provide all lines of property-casualty insurance to U.S. consumers and businesses, writing more than $117 billion annually in U.S. property-casualty premiums and approximately $225 billion annually in worldwide property-casualty premiums. Our members have a significant interest in the Consultative Document relating to cross-border recognition of resolution actions.

While AIA appreciates the complex and significant issues involved in cross-border recognition of resolution actions for financial institutions, AIA's expertise and experience relates to the resolution of U.S. property-casualty insurers. AIA's comments, accordingly, are directed at resolution of property-casualty insurers in the United States and the need to ensure that global frameworks regarding cross-border recognition of resolution actions do not inappropriately interfere with the resolution of U.S. property-casualty insurers or with ongoing, regulated, business operations of U.S. property-casualty insurers.

I. U.S. Property-Casualty Insurers Are Extensively Regulated to Enhance Policyholder Protection

Property-casualty insurers are extensively regulated under U.S. state law and are closely supervised by state insurance authorities. As a result, property-casualty insurers present very low risk to the financial system. Accordingly, property-casualty insurers engaged in traditional insurance activities do not present significant risk to financial stability either within the U.S. or globally.

Insurance firms do not present leverage to the economy, and do not have an infrastructure maintenance function. As the International Association of Insurance Supervisors has noted, "there is little evidence of insurance either generating or amplifying systemic risk, within the financial system itself or in the real economy." [1] Insurance companies operate under a different business model than other financial firms, based on an "inverted cycle of production"[2] where premiums are received up-front. The property-casualty industry model is premised upon collecting sufficient premium in advance to fund covered claims. Hence, there is less need to borrow and consequently a lower likelihood of becoming highly leveraged.

The insurance business model helps shield property-casualty insurers from the "run on the bank" scenario frequently used to describe the contagion effect of systemic risk. Unlike customer deposits held by banks, payment of claims under an insurance policy depends on the occurrence of a covered event. Therefore, as a practical matter, insurance consumers do not have "on demand" access to insurance assets as they would with other financial institutions.

The financial regulatory standards and metrics in place for U.S. property-casualty insurers underscore the financial strength of the property-casualty insurance sector and the soundness of its business model. State regulators impose financial supervision on the operating insurance companies themselves, so that property-casualty companies will always be in a position to meet their obligations to policyholders. There are also capital and regulatory penalties that discourage risky financial behavior and excessive leverage by U.S. property-casualty insurers.

Insurance companies are extensively regulated to provide protection to policyholders and to other claimants under property-casualty policies, such as injured workers. It is imperative that resolution actions in other jurisdictions do not inappropriately interfere with the workings of the U.S. property-casualty regulatory system. Resolution actions in these jurisdictions should not interfere with the business operations of U.S. property-casualty, potentially imperiling the strength of the insurers and the policyholder protections at the core of the U.S. regulatory system.

II. State Receivership Law Applies to the Resolution of U.S. Property-Casualty Insurers

State laws set forth detailed receivership and liquidation procedures for U.S. insurance companies. When a state regulator concludes that an insurer is in serious financial trouble, the regulator will usually first place the insurer in receivership proceedings. In a receivership proceeding, the company continues to exist but the receiver manages the insurer's existing business and is responsible for the paying of all claims. The goal of a receivership is to

[1] "Position Statement on Key Financial Stability Issues," International Association of Insurance Supervisors, p.2 (IAIS Paper)(October 25, 2009).
[2] "Systemic Risk and the Insurance Sector," International Association of Insurance Supervisors, p.2 (IAIS Paper)(October 25, 2009).

rehabilitate the insurer so that the insurer can once again exist as a fully-functioning insurer outside the management of the state-appointed receiver.

If receivership is successful, the company is removed from receivership and is permitted to resume normal business operations. In other situations, however, the receiver determines that further efforts to rehabilitate the insurer would be ineffective and petitions a court for an order of liquidation with a finding of insolvency. If the state court grants the order of liquidation, the insurance company essentially ceases to exist and the liquidator begins proceedings to marshal all the assets of the insurer and sells them to raise capital to pay all creditors of the insolvent insurer.

i) The State Guaranty Fund System Provides Timely Payments to Policyholders and Claimants

The primacy of policyholder protection under U.S. law is further enhanced by the state guaranty fund system. The obligation of a state guaranty fund to pay an insolvent insurer's policy obligations (subject to certain statutory limits and exclusions) is triggered by the state court's order of liquidation with a finding of insolvency. Once the order is filed and a finding of insolvency is made, a state guaranty fund steps into the shoes of the insolvent insurer and pays the insurer's policyholder and third-party claims. Payments to policyholders and claimants under the policy, thus, are paid outside the liquidation proceeding, in a timely fashion without the typical delays necessarily attendant to liquidations.

The receivership and liquidation proceedings, together with the guaranty fund system, has worked well and without problems in maintaining the stability of the insurance industry while ensuring that policyholders and third-party claimants receive payments under the insurance contracts in a timely and appropriate manner.

ii) The Dodd-Frank Act Continues the State Receivership Role in U.S. Insurer Receiverships

The recent enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act) acknowledges the role of state receivership and liquidation proceedings and the guaranty fund system in ensuring policyholder protection and providing stability in the insurance sector. Under the Dodd-Frank Act resolution of insurers in the United States remains under state receivership law. Title II of the Dodd-Frank Act establishes a procedure for the appointment of the Federal Deposit Insurance Corporation ("FDIC") as receiver of a failing financial company that poses a significant risk to the financial security of the United States. Nonetheless, in order to deal with the uniqueness of the insurance industry, the Dodd-Frank Act has separate provisions that address treatment of insurance companies under Title II's orderly liquidation process. Section 203(e) provides that if a covered financial company is an insurance company, or if an insurance company is a subsidiary or an affiliate of a covered financial company, liquidation of the insurance company must be conducted in accordance with state law and not by the FDIC.

III. Cross-Border Resolution of Financial Institutions Must Not Interfere with the State Regulatory and Receivership Oversight of U.S. Property-Casualty Insurers

It is imperative that cross-border resolutions of financial institutions do not interfere with the regulatory and receivership framework applicable to U.S. property-casualty insurers. Based on both the property-casualty business model and the extensive regulatory oversight applicable to them, property-casualty insurers do not pose systemic risk and policyholder protection is safeguarded. In a situation where a property-casualty insurer faces financial distress, well-developed state receivership procedures make sure the insurer is either rehabilitated or, if appropriate, liquidated. If liquidation is necessary, state guaranty funds quickly step into the shoes of the insolvent insurer and make timely payments to policyholders, injured workers and third-party claimants.

The Dodd-Frank Act recognizes the pivotal role state receivership, together with the state guaranty fund system, play in enhancing policyholder protection and authorizes the current state system to continue to handle the resolution of insurers. Similarly, cross-border jurisdictions involved in resolution of financial institutions should not encroach on the regulatory and resolution framework applicable to U.S. property-casualty insurers.

AIA thanks you for your attention to these issues.

Sincerely,

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