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

Re: Consultative Document: Effective Resolution Strategies and Plans for Systemically Important Insurers

Dear Chairman Carney:

The American Insurance Association ("AIA") welcomes the opportunity to comment on the Financial Stability Board's ("FSB") Consultative Document: Effective Resolution Strategies and Plans for Systemically Important Insurers.

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 resolution strategies and plans for systemically important insurers.

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 any global framework for resolution strategies and plans does 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 global 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 plans and strategies in other jurisdictions do not inappropriately interfere with the workings of the U.S. property-casualty regulatory system. Resolution plans 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.

i) Policyholder Protection must be a Paramount Goal for Insurer Resolution Strategies and Plans

The consultative document states "Authorities should develop resolution strategies with the aim of maintaining financial stability and to the fullest extent possible, protecting policyholders when an insurer fails." AIA, of course, strongly supports the need for maintaining financial stability; however, protecting policyholders must remain a paramount objective. AIA objects to the consultative document's use of the phrase "to the fullest extent possible" because it could

[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).

be interpreted to limit the priority of policyholder protection. In our view, policyholder protection is a paramount goal and is itself critical to maintaining financial stability. Indeed the reason insurers are heavily regulated in the United States is to enhance policyholder protection. The consultative document should not be subject to an interpretation suggesting policyholder protection is a goal that may be sacrificed. We would suggest that the language on page 10 of the consultative document be modified to read "Authorities should develop resolution strategies with the aim of maintaining financial stability and~~, to the fullest extent possible,~~ protecting policyholders when an insurer fails."

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 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) State Guaranty Funds should be part of Developing and Assessing Resolution Strategies and Plans

In the United States, state guaranty funds play an integral role in the resolution of insolvent insurers. State guaranty funds have played a significant role over the past four decades in ensuring that policyholders and claimants are paid claims in a timely and appropriate manner according to state laws when an insurer becomes insolvent. The consultative document should recognize the vital role that policyholder protection schemes, such as state guaranty funds in the United States, can play in developing and assessing resolution strategies. Collaboration and planning by regulators and the guaranty fund system has consistently ensured a smooth transition to liquidation and coverage of policyholder claims by the guaranty fund system when there is a subsequent insurer insolvency. AIA recommends that the consultative document specify that policyholder protection schemes can play an important role in developing and assessing resolution strategies and should be a part of crisis management groups and other coordination efforts.

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 global resolution plans 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, U.S. 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 insurers 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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