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

RE: Consultative Document
Effective Resolution of Systemically Important Financial Institutions

Dear Chairman Draghi:

The American Insurance Association ("AIA") appreciates the opportunity to comment on the Financial Stability Board's ("FSB") Consultative Document, "Effective Resolution of Systemically Important Financial Institutions."

AIA represents approximately 300 leading United States insurance companies that provide all lines of property-casualty insurance to consumers and businesses in the U.S. and throughout the world, writing more than $117 billion annually in premiums. Our members have a significant interest in the Consultative Document.

Property-Casualty Insurance Companies Do Not Pose a Threat to Financial Stability.

AIA recognizes the FSB's interest in improving the capacity of authorities to resolve systemically important financial institutions ("SIFIs") without systemic disruption and without exposing taxpayers to risk of loss. As a trade association representing U.S. property-casualty insurers, AIA notes that U.S. property-casualty insurers are extensively regulated under state law and closely supervised by state insurance authorities. As a result, property-casualty insurers pose very little risk to the global financial system. Insurance firms do not present leverage to the economy, and do not have an infrastructure maintenance function. For a number of reasons, "there is little evidence of insurance either generating or amplifying systemic risk, within the financial system itself or in the real economy."[1] Accordingly, AIA believes that property-casualty insurers engaged in regulated insurance activities will not pose a significant risk to financial stability either within the U.S. or globally.

[1] Position Statement on Key Financial Stability Issues," International Association of Insurance Supervisors, p. 2 (IAIS Paper) (Oct. 25, 2009).

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.

All these elements combine to eliminate the potential for a property-casualty insurer engaged in the regulated business of insurance to be a source of financial instability.

State Receivership Proceedings and the Guaranty Fund System Provide Effective Resolution of Property-Casualty Insurance Companies.

The Consultative Document states that corporate "liquidation procedures are not well suited to deal with the failure of major banks and other financial institutions."[3] While the prior sections set forth why U.S. property-casualty insurers do not pose a systemic risk to global financial stability, in any event, the current state-based resolution process for U.S. property-casualty insurers is highly developed, has worked well and without problems for decades and best promotes financial stability while at the same time making sure insurance policyholders and other claimants and creditors are protected and taxpayer money is not put at risk.

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 difficulty, the regulator will usually first place the insurer in receivership proceedings. In a receivership proceeding, the company continues as a going concern but the receiver, who is appointed by the state regulator, manages the insurer's existing business and is responsible for the payment 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

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[2] "Systemic Risk and the Insurance Sector," International Association of Insurance Supervisors, p. 2 (IAIS Paper) (Oct. 25, 2009).

[3] Consultative Document, "Effective Resolution of Systemically Important Financial Institutions," p. 8. (July 19, 2011).

finding of insolvency. If the state court grants the order of liquidation, the insurance company essentially ceases to do business and the liquidator begins proceedings to marshal all the assets of the insurer, selling them to raise capital to pay all creditors of the insolvent insurer.

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 as they arise. Payments to policyholders and claimants under the policy thus are paid *outside* the liquidation proceeding in a timely fashion.

The receivership and liquidation proceedings together with the guaranty fund system have worked well to maintain the stability of the insurance system while ensuring that policyholders and third-party claimants receive payments under an insolvent carrier's insurance contracts in a timely and appropriate manner.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), enacted in the U.S. to help preserve financial stability and address systemic risk, acknowledged the role of state-based insurance receivership and liquidation proceedings and the guaranty fund system in protecting stability in the insurance sector. 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 SIFI. 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. 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 is to be conducted in accordance with applicable state law, not federal law.[4]

The Consultative Document should mirror the Dodd-Frank Act and specify that any new resolution authority to be created to deal with global systemically important financial institutions ("G-SIFIs") will not displace the current receivership and liquidation process and state guaranty fund system already in place for U.S. property-casualty insurers. The Consultative Document should specify that if the G-SIFI is a U.S. insurance company, or if a U.S. insurance company is a subsidiary or an affiliate of a G-SIFI, any potential resolution of the insurance company is to be conducted in accordance with applicable U.S. state receivership or liquidation law.

Recovery and Resolution Plans are Unnecessary for U.S. Property-Casualty Insurers Considering the Regulatory System Applicable to Them.

The Consultative Document discusses the drafting of recovery and resolution plans for G-SIFIs. The drafting of the recovery plan is the responsibility of the G-SIFI and the drafting of the resolution plan is the responsibility of the regulating authorities. The recovery plan is to serve as a guide to the recovery of a firm in financial distress. The resolution plan is intended to facilitate the effective use of the resolution authority's resolution powers to make feasible resolution without severe systemic disruption and without exposing taxpayers to loss.[5]Because insurers are subject to state-based receivership laws, it

[4] Dodd-Frank Act §203(e).
[5] Consultative Document, "Effective Resolution of Systemically Important Financial Institutions," pp. 53-60. (July 19, 2011.

is impossible for them to prepare resolution plans that would meet informational content requirements that might be established. State-appointed receivers have plenary authority over the disposition of assets, liabilities, and affairs of an insurance company in receivership. As a result, preparation of a resolution plan would necessarily depend on predicting how the receiver intends to exercise his or her statutory authority.

In this context, U.S. insurers are in a position with regard to resolution matters that is virtually identical to that of insured depository institutions for which the Federal Deposit Insurance Corporation ("FDIC") is appointed receiver under the Federal Deposit Insurance Act ("FDIA"), with the FDIC having similar plenary authority.[6] Proposed regulations following the Dodd-Frank Act's parallel provisions for the filing of so-called "living wills" thus recognizes that resolution plans submitted by bank and savings and loan holding companies will not address resolution of the depository institution subsidiaries because of the primacy of the FDIA and the role of the FDIC as receiver. Accordingly, AIA strongly urges that, in view of the role of state insurance laws relating to resolution of insurers, the Consultative Document clarify that U.S. insurers are not required to submit a report regarding the insurer's plan for rapid and orderly resolution in the event of material financial distress at or failure of the company.

In this connection, page 11, under **Scope of application**, the document states that: "…to the extent that insurers conduct activities which are bank-like, the application of banking sector resolution tools to such activities rather than to the insurer as a whole or to its core traditional insurance business may be appropriate." We certainly agree with the principle that applying non-insurance resolution tools to the regulated business of insurance would not be appropriate or beneficial. However, because the term "bank-like activities" could cover activities such as investing and lending, we are concerned that the provision may be interpreted to apply to routine powers exercised by insurers in the ordinary course of business. Such a misreading could lead to the inappropriate application of banking resolution procedures to a broad range of activities engaged in by insurance companies. We think this might lead to confusion and uncertainty as to what regulatory scheme will apply to which activities of an insurer and could even lead to gaps in regulation.

A better approach is to recognize that insurance regulators have the responsibility and authority to regulate all activities carried out by an insurance company in connection with the business of insurance. Although certainly a consideration, the ultimate question in our view is not whether activities are "core traditional insurance business," but whether even non-core or non-traditional activities engaged in by an insurance company are subject to adequate supervision and regulation by insurance regulators. If they are, then a sounder approach is to subject the insurance institution and all of its regulated activities to the proven effective recovery and resolution provisions that have long been part of U.S. insurance regulation.

Finally, we believe the document should restate at several points that its recommendations are to be applied only to carefully defined Systemically Important Financial Institutions. This will help avoid any confusion on the part of readers.

[6] 12 U.S.C. § 1821(d).

AIA thanks you for the opportunity to comment and for your attention to these issues.

Respectfully submitted,

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