

## **RAA LAW BULLETIN # 09-82**

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**SUBJECT:** Treasury Releases Financial Reform Legislative Package Including Office of National Insurance

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Yesterday the Administration delivered proposed legislation to Capitol Hill that would require consolidated supervision and regulation of financial firms. Included in proposals is legislation to create the Office of National Insurance (“ONI”).

The Treasury proposals provide a regulatory regime to monitor, mitigate and respond to risks in the financial system. Copies of the proposed legislative language are attached to this e-mail for your information. They include: (1) the Financial Services Oversight Council Act of 2009; (2) the Bank Holding Company Modernization Act of 2009; (3) the Bank Holding Company and Depository Institution Regulatory Improvements Act of 2009; (4) the Investor Protection Act of 2009; (5) an amendment to the Federal Reserve act; and (6) the Office of National Insurance Act of 2009. This bulletin will discuss the Financial Services Oversight Council, changes to the Bank Holding Company Act and the ONI.

### **Office of National Insurance**

The Office of National Insurance Act proposed by Treasury is very similar to the Office of Insurance Information legislation introduced by Representative Kanjorski in May. Key differences between the two pieces of legislation include the provisions related to the authority to enter into international agreements and the preemption of state laws.

Treasury’s proposal would create an Office of National Insurance within the Treasury Department tasked with monitoring the insurance industry to identify gaps in regulation that could contribute to a systemic crisis. The office would have the authority to: (1) collect information from insurers, (2) recommend that an insurer be designated as a “Tier 1 financial holding company (which would trigger “systemic risk” oversight by the Federal Reserve), (3) assist in administering the Terrorism Risk Insurance Program, (4) coordinate Federal efforts and establish Federal policy on prudential aspects of international insurance matters, (5) make preemption determinations, and (6) consult with the states regarding insurance matters.

On international insurance matters, the Treasury proposal explicitly authorizes the Secretary of the Treasury to negotiate and enter into International Agreements on Prudential Measures on behalf of the United States. The Director of the ONI also is given specific authority to assist the Secretary in this regard. However, unlike the Kanjorski OII legislation, the scope of authority in the Treasury proposal is tied to

“prudential aspects” on international insurance matters and the agreements that the ONI references are “International Insurance Agreements on Prudential Measures.” Treasury’s proposed legislative language does not define “prudential measures.”

The ONI has the authority to make determinations that a state insurance measure is preempted. The preemption language is as follows:

A State insurance measure shall be preempted if, and only to the extent that the Director determines, in accordance with this subsection, that the measure—

(A) directly or indirectly treats a non-United States insurer domiciled in a foreign jurisdiction that is subject to an International Insurance Agreement on Prudential Measures less favorably than it treats a United States insurer domiciled, licensed, admitted, or otherwise authorized in that State; and

(B) is inconsistent with an International Insurance Agreement on Prudential Measures.

The preemption authority is limited to instances where there is an inconsistency with an International Insurance Agreement on Prudential Measures and allows the Director of the ONI to make a preemption determination when a state measure “directly or indirectly treats a non-United States insured domiciled in a foreign jurisdiction that is subject to an International Insurance Agreement on Prudential Measures less favorably than it treats a United States insurer.” The Kanjorski OII legislation allowed a preemption determination when a state measure treated a non-U.S. insurers “more or less” favorably than a U.S. insurer. Despite the ONI’s authority to establish federal policy on prudential aspects of international insurance matters, a preemption determination can only be made by the ONI when a state measure treats a non-U.S. insurer less favorably than a U.S. insurer and the measure is inconsistent with an international agreement.

The Treasury proposal streamlines the preemption provisions by eliminating the stay provisions from the Kanjorski OII legislation which allow a stay of preemption if (1) maintaining the state measure is necessary for prudential reasons, (2) preemption will result in any need to establish a Federal regulatory role by the Office over an entity involved in the business of insurance, (3) or preemption will result in a gap in financial or market conduct regulation. The Treasury proposal also eliminates provisions from the Kanjorski OII legislation which allow Congress to intervene to nullify a preemption determination.

In making a preemption determination under the Treasury proposal, the ONI must publish a notice of potential inconsistencies and permit interested parties to comment. Preemption then becomes effective after a “reasonable period of time” as determined by the ONI. A state insurance measure is defined in the Treasury proposal to mean any state law, regulation, administrative ruling, bulletin, guideline, or practice relating to or affecting prudential measures applicable to insurance or reinsurance. Again, the Kanjorski OII legislation does not contain the reference to “prudential measures.”

## **Systemic Risk Regulation**

Treasury's legislative proposals also included systemic risk regulation aimed at financial services. The proposals consolidate supervision and regulation by creating a regulatory framework for Tier 1 Financial Holding Companies. A financial firm can be designated a Tier 1 Financial Holding Company based on its size, leverage and interconnectedness. The framework requires Tier 1 Financial Holding Companies to conform their activities to the Bank Holding Company Act within 5 years of designation. The proposals also require prompt corrective action when a Tier 1 Financial Holding Company's capital levels decline.

## **Financial Services Oversight Council**

Another piece of Treasury's proposal creates a Financial Services Oversight Council to monitor and report emerging risks. The Council will be made up of one member from each of the principal federal financial regulators. Although there is no separate insurance member, insurance will be represented by Treasury (the Secretary of the Treasury also serves as Chairman of the Council). This council replaces the President's Working Group on Financial Markets.

## **Political Outlook**

House Financial Services Committee Chairman Frank and Subcommittee Chairman Kanjorski have not indicated a timeframe when they will take up this legislation. The House of Representatives leaves on July 31<sup>st</sup> for the August Recess and returns on September 8<sup>th</sup>. The Committee's agenda is quite full in September with other financial service reform priorities, thus we expect the earliest ONI legislation would be considered by the Committee would be late September. We will keep you apprised of developments on the timing of this issue and other legislative proposals related to financial services that impact insurance.