THE REGULATOR™
INSURANCE REGULATORY EXAMINERS SOCIETY

Is state insurance regulation dead?

A REGULATOR SPECIAL REPORT

Oh, what a tangled web we weave
when state regulation we try to leave

by Scott Hoober
Special to THE REGULATOR

Is state regulation of insurance companies obsolete?

The question is being asked, in different ways by many people who wonder if states can keep up with complex global markets, electronic commerce over the Internet and the merging of banking and insurance services. So THE REGULATOR recently asked a panel of experts to tell us whether they believe the end is near for state control. Few of them do. But as you'll see in these pages, we received some thought-provoking answers — and new questions.

It's not a matter of state regulation being dead, writes David Snyder of the American Insurance Association. He says a better question is, *"Which insurance regulation should be alive and which dead?"* Snyder argues for a greater focus on solvency and for a severe pruning of the "regulatory overgrowth" associated with rate and form approvals.

"Congress should not fall into 'either/or' thinking," says J. Robert Hunter of the Consumer Federation of America. There are some things states do better, Hunter adds, but globalization, the Internet and the Frankel case argue for a federal role: *"Can Wyoming's 28 staffers really control that insurance web page in Addis Ababa?"*

Now just wait a minute, counters, George Nichols III, Kentucky's commissioner of insurance and NAIC vice president. He believes most consumers would never swap the personal touch they get from their local insurance regulator for a giant, faraway federal bureaucracy. "We know where Campbellsburg, Kentucky, is," Nichols writes, " and we are prepared to help. . .I cannot imagine the Federal Reserve or the Office of Comptroller making such an effort. Inside the Washington Beltway, they might have trouble finding Campbellsburg on the map."

The debate continues over who is best equipped to serve and protect the insurance-buying public. We thank our panel for sharing their thoughts. Your replies and rebuttals are welcome.

NOVEMBER 1999

Is state insurance regulation dead?

The Regulator™

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THE REGULATOR is published every other month by the
INSURANCE REGULATORY EXAMINERS SOCIETY™

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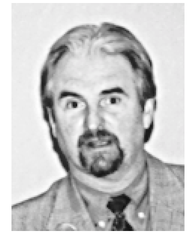
From the Editor

by Wayne Cotter



I guess you can say Marty Frankel inspired this special "state v. federal" issue of *The Regulator*. If you don't know Marty Frankel, you should. He's the "investment advisor" who allegedly absconded with hundreds of millions dollars of insurance company money and is currently fighting extradition from a German jail. Hwe's also the fellow who prompted Rep. John Dingell (D-Michigan), a longtime critic of state insurance regulation, to take a fresh look at the current insurance regulatory structure, and prompted IRES to ask, "Is State Insurance Regulation Dead?"

The changes that occur in the insurance regulatory system over the next few years will have a profound impact on us for the remainder of our professional careers. So please, take the time to read what our contributors are saying and let us know what you think.

In addition, you may want to consider the following:

Before choosing federal regulation, a few points to remember

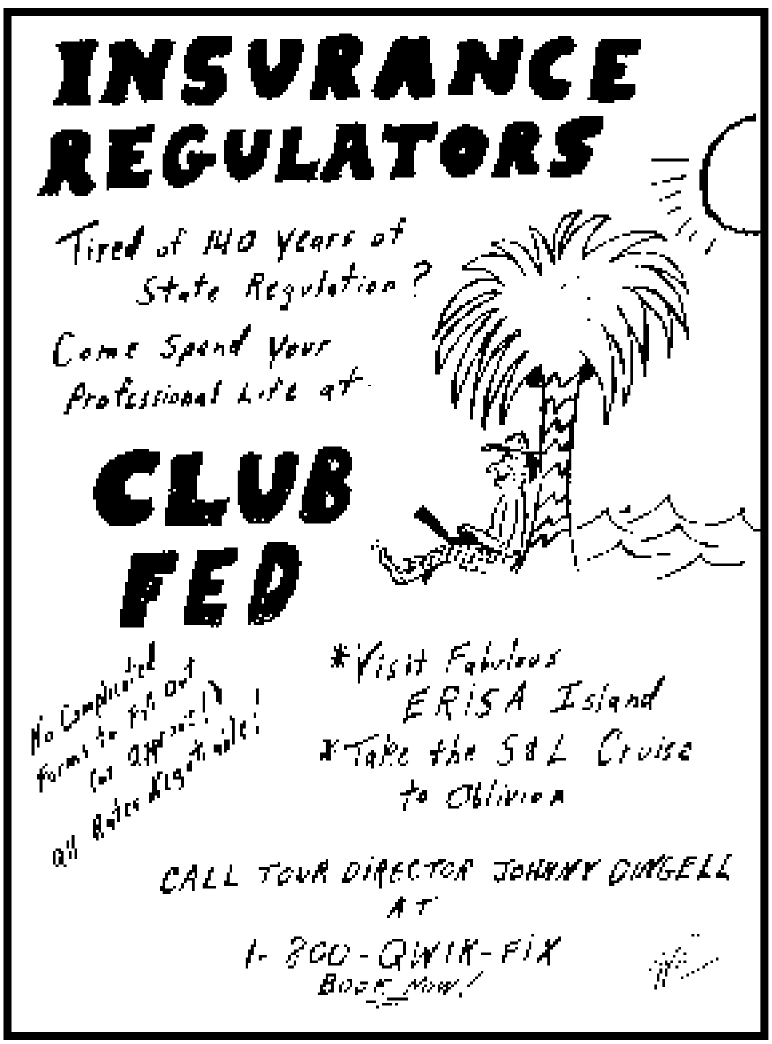
• If you're contemplating a change in the existing regulatory structures due to Marty Frankel, think again. No matter how strong the regulatory structure, there will always be the Marty Frankels of the world looking to game the system. Case in point: Another Marty (this time global investment manager Martin A. Armstrong) recently was accused of bilking Japanese investors of close to $1 billion, a sum far exceeding estimates of Frankel's ill-gotten gains. Last time we looked, the securities industry was regulated primarily by the federal government. Who has been calling for an overhaul of that system?

• And if memory serves us correctly, wasn't it federal regulators and legislators who prolonged the Savings & Loan debacle of the late 1980s? Marty Frankel's gains are chump change compared to the $200 billion in losses that resulted from the failure of more than 1,100 thrifts.

• A very unsettling story recently emerged regarding abuses of the banking regulatory structure. (See *The New York Times*, 9/16/99.) It seems the Clinton Administration was disturbed over modifications to the Community Reinvestment Act contained in the proposed H.R. 10 bill and sought out banking executives willing to submit testimonials buttressing the Administration's position. The Office of the Comptroller of the Currency, according to the Times, *"instructed bank examiners in field offices to seek testimonials from bankers about the Community Reinvestment Act."* Bank examiners contacted at least a dozen banks, with little success. One bank did, however, feel uncomfortable enough to question the integrity of the process and complain to Senate Banking Committee staffers. The bank was in the midst of a routine financial examination at the time of the request and had the distinct impression that its examination results could hinge on its willingness to comply. The OCC quickly withdrew its instructions and acknowledged its "mistake" once Senate Committee members expressed concerns.

• Finally, you may remember that last fall the Federal Reserve Bank convinced a consortium of key investment banks to commit $3.6 billion to stave off the collapse of Long-Term Capital Management (LTCM), a 4-year-old hedge fund. Investment banks seldom reach a quick consensus on any matter, let alone one of such magnitude. In this case, however, *in a matter of days* the banks had quietly paid up, rescued the fund, and restored market confidence. One can only surmise that this one must have been a real no-brainer—*LTCM cannot go down.* As of this writing, the fund is still liquidating assets and returning capital to the consortium. The big questions, however, remain: How could *one* hedge fund within the space of four short years become "too big to fail" and what has been done to prevent a recurrence?

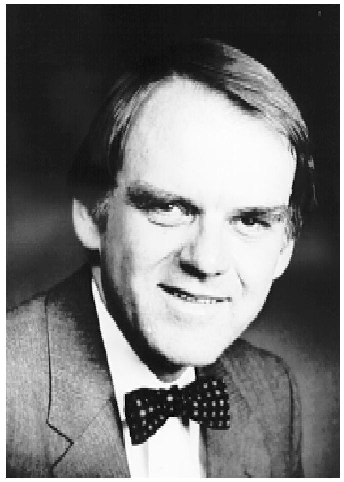
Let us know when you hear some answers. ■



Tell us what you think about the current state of state regulation. Is a federal approach a better way to go? Can a dual regulatory system work? Did our pundits cover all the bases? Who hit the home runs? Who struck out? E-mail your responses to Wayne Cotter at quepasa@sprintmail.com or mail to the REGULATOR's Olathe, Kansas, address (see page 2 for full address). Your responses will be printed in upcoming issues.

J. Robert Hunter

Is state insurance regulation dead?



Consumers don't care who regulates insurance. What consumers do care about is the effectiveness of regulation. Research over the last 20 years by the General Accounting Office, the Consumer Insurance Interest Group (a coalition of consumer groups and industry groups) and CFA has revealed a mixed record for the states in regulating insurance products. So the record to date is spotty at best.

But what about the future? Do current economic trends have positive or negative implications for the future effectiveness of state regulation?

Trends Undermining State Effectiveness include:

- Globalization/International trade agreements. The trend is for more large and complex global players dominating the insurance market. These arrangements are beyond the capacity of most states. No state can enter into treaty with another nation if such is needed to make regulation work.
- Merger Mania. Huge insurance providers are emerging. Understaffed states can't keep up with these giant, complex entities. They are also "too big to fail" given the non-funded guarantee systems in place.
- Financial services walls tumbling down. Banks now act as insurance agents. Where does the federal bank regulator's role end and the state regulator's begin?
- Internet and other electronic wizardry. Billions of dollars daily cross international borders in milliseconds. Sales of insurance take place on the World Wide Web. Can Wyoming's insurance department's 28 staffers really control that insurance web page in Addis Ababa?

The Martin Frankel case shows the strain for state regulation from these trends. Electronic wheeling and dealing, lack of coordination between financial regulators (SEC busted Frankel in 1990) and the foreign (London and Vatican) dealings appear to have been beyond early state detection and action.

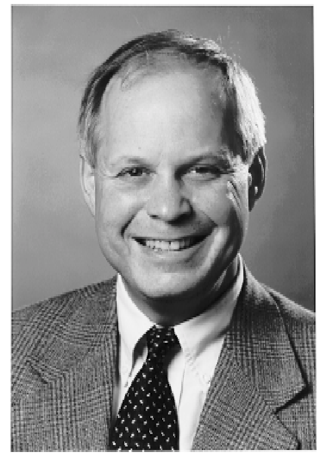
What can be done to assure effective insurance regulation?

Congress should study state insurance regulation to determine if a federal role is needed. It has been 20 years since GAO last looked at insurance regulation. In its review, Congress should not fall into "either/or" thinking. The federal role might be optional, partial, minimum standards, technical assistance, or some other less than total role. While my view is that the federal government should not replace all of state regulation, since there are some things the states can do better (e.g. handle complaints and supply consumer information), even that should be studied.

continued on next page

Mr. Hunter worked 10 years in the private sector and then 12 years in government (Administrator of the Federal Insurance Administration and Texas Insurance Commissioner) and 18 years as a consultant to consumers and, pro-bono, in the consumer sector (President of the National Insurance Consumer Organization and, currently, Director of Insurance for the Consumer Federation of America).

David Snyder



State regulation of insurance is clearly not dead. But both the question in the title and the answer miss the real issue. A better question is: "Which insurance regulation should be alive and which dead?"

Regulation for solvency is the most important function of insurance regulation. Having the financial wherewithal to pay claims is inherent to the ability of insurers to fulfill their obligations under their contracts and to play their socially beneficial role of compensation. Unfortunately, insurance regulation has expanded in most States far beyond this solvency regulation to the extent that some State requirements undermine, rather than enhance insurer solvency.

Insurance regulation in most States extends to rates, forms, cancellation and non-renewal and virtually everything insurers do or don't do. Much of this regulatory overgrowth could be cut back with two main benefits: counterproductive regulation and its costs could be reduced and regulatory resources could better be focused on solvency regulation.

Insurance rate regulation, or price control, is alive and well in many States, but has been abolished in every other industry and product in the U.S. and around the world for two simple reasons: it doesn't work and it ultimately hurts consumers. Competition does indeed provide the best products at the least possible price. It is true for insurance, as well as other products.

While State regulation for solvency should be vigorous, it often takes a back seat to other more attractive regulatory activities. Meanwhile, counterproductive regulation of rates, cancellation and non-renewal and forms, which are best regulated by the marketplace, is alive and well. The answer to the real question, in my view, is: "While some insurance regulation should be alive, some should not."

Mr. Snyder is Assistant General Counsel for the American Insurance Association. He previously worked for the Pennsylvania Insurance Department and other state and federal agencies. The American Insurance Association is a trade organization representing more than 300 major insurance companies that provide all lines of property/casualty insurance.

Hunter *continued from page 4*

State and federal regulators must look beyond "turf" issues to the needs of consumers as this review progresses. It is certain that the states could use federal help in some areas, but the fear of "the camel's nose," may blind the states from taking advantage of this help. After all, camels are good to have around when the load is too heavy.

Even if there were not these troubling trends, Congress has a duty to review the massive delegation embodied in the McCarran-Ferguson Act to determine both how it is working and will work in the future. CFA believes that only proper use of the strengths of both state and federal agencies can assure effective insurance regulation in the 21st Century.

Joseph Belth

Is state insurance regulation dead?

State regulation of the insurance business is not dead. Political realities assure its survival. In its long history it has weathered numerous challenges, and it will continue to do so even in the face of moaning and groaning over revolutionary developments and Monday morning quarterbacking about the Marty Frankels of the world. Also, despite the superficial attractiveness of a national approach, it is doubtful that federal regulation would be more effective.

A more important question is whether keeping state regulation alive serves the public interest. The answer depends on the manner in which state regulation adapts to massive changes that have occurred and will continue to occur in business and technology.

State regulators must be willing to work with federal authorities and even with officials in other countries to develop responses to the challenges of a global economy.

To do so, state regulators need not only the support of their legislatures to provide adequate funding, but also the support of the insurance business. When shortsighted insurance companies take actions that undermine state regulation—such as lobbying for the infamous redomestication provision in the federal financial services bill—they do severe damage not only to the institution of state regulation but also to their own long-term interests.

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Joseph M. Belth, PhD, is the editor of the Insurance Forum, Elletsville, Indiana. Mr. Belth is professor emeritus of insurance in the Kelley School of Business at Indiana University, Bloomington.

Michael Duncan

State regulation is alive and well and living in Ashtabula, Ohio; Yakima, Washington; Lubbock, Texas; and every other community in the United States where insurance companies compete for business and consumers demand better coverage, outstanding service and fair prices.

Currently, state regulation is being questioned because of modernization and globalization of financial services. The difficulties of dealing with 51 jurisdictions is becoming more apparent and of greater concern. However, the NAII sees as flawed the belief that these concepts require federal regulation.

It is our belief that for property-casualty insurance, all markets are local. The products, the price, the underwriting and claims payment processes are affected by local conditions and sometimes appropriately differ by state. This is not to say that all aspects of regulation should vary by state. A main concern driving globalization is the ability to access markets. In that regard, uniformity and simplicity of licensing insurers and their producers is appropriate. The states can accomplish this by adoption of a model law in development by the NAIC. No federal solution is necessary.

But, in areas where differences are appropriate, states should reflect local conditions and values. A benefit of doing this follows the fundamental principle of the insurance business – spread the risk. Bad regulation in one state does not poison the regulatory environment in every other state. Ultimately, through market pressure or political pressure, state legislators or regulators will amend or repeal regulation that damages the competitive environment or that hurts consumers.

Federal regulation, on the other hand, forces insurers and consumers to put all their eggs into the basket of one national regulator. Experience shows that such a regulator is commonly insulated from public accountability.

So, on balance, we say that no case has been made for federal regulation; dual regulation would be the worst possible outcome; and state regulation makes sense because property-casualty insurance is clearly affected by local conditions.

A careful review of the track record of insurance regulation since adoption of the McCarran-Ferguson Act in 1945 reveals a number of points in history with critics saying that state regulation is dead and that some type of federal regulation is "just around the corner." Yet each and every time state regulation has responded to the challenge and, most important, kept the prerogative to regulate the business of insurance where it belongs – with state public policy makers who are close to the citizens and their markets.

When it comes to periodic criticism of state regulation of insurance, I am reminded of the comment made by Winston Churchill about the burdens of governing in a democracy. He stated that, "Democracy is the worst form of government, except for all the others." While state regulation is not perfect, it is far better than the alternative.

Michael P. Duncan is the senior vice president, secretary and general counsel of the National Association of Independent Insurers. Prior to joining NAII, he served as vice president and assistant general counsel of Allstate Insurance Company. He is a former Director of Insurance for the state of Illinois.

George Reider

regulation dead?

The National Association of Insurance Commissioners supports the efforts to modernize and improve federal laws that govern how banking, insurance and securities products are regulated in the United States. Achieving that goal, however, will require that Congress preserve current state regulatory authority to protect all Americans who purchase or depend upon insurance for financial security.

There is no federal regulatory agency for regulating the business of insurance. If the federal government prevents the states from supervising insurance adequately, this vital consumer protection won't get done well at all. My home state of Connecticut was involved last year in the regulatory approval process of the merger between Travelers Insurance and Citibank. The ongoing review of Citigroup is an excellent example of successful functional regulation.

Individual states and their citizens bear the costs associated with regulating insurance providers, including the costs of any insolvencies that occur. State governments thus have a powerful incentive to do the job well, and the record shows they have done so.

> **"[The NAIC] supports the efforts to modernize and improve federal laws that govern how banking, insurance and securities products are regulated. Achieving that goal, however, will require that Congress preserve current state regulatory authority to protect all Americans."**

While Congress and industry have been talking about modernizing financial services regulation, state insurance departments are working through the National Association of Insurance Commissioners to accomplish much greater uniformity and efficiency among themselves. New technology is being used to allow constant communication and updated data sharing on key licensing, enforcement and rate filing requirements. State departments are also signing reciprocity agreements dealing with agent licensing to eliminate needless redundancy.

The state insurance regulators take pride in their work, their record of accomplishments and the ongoing efforts to keep abreast of changes in the marketplace, which affect insurers and consumers.

Mr. Reider is President of the National Association of Insurance Commissioners and Connecticut Commissioner of Insurance.

Peter Kinzler

Is state insurance regulation dead?

Yes, with respect to auto insurance — unless state regulators change their historical stripes and start advocating for insurance that meets consumers' needs for more choice, lower costs and better compensation of serious injuries.

Auto insurance is a disaster in most states today. Unlike the rest of the American economy, auto insurance is a plain vanilla product in 47 states. In 37 states, it is a lawsuit-based tort system that pays plaintiff and defense attorneys nearly twice as much as it pays injured people for their legitimate medical and work loss expenses. It is slow to pay people and pays out only 14.5 cents on each premium dollar for real medical bills and work losses. Worst of all, it pays the most seriously injured people only 9 cents for each dollar of economic loss.

Ten states mandate different forms of no-fault insurance. They all provide more timely compensation of economic loss that is more according to need. However, the majority of them have been weakened by trial bar opposition to the point where they are too costly because they are supporting both the tort system and a no-fault system. Only three states permit a choice between tort and no-fault options.

Regulators as well as trial lawyers, defense attorneys and many insurers are responsible for not giving consumers what they need and deserve. Each group is more concerned with protecting its own turf rather than the welfare of motorists. Regulators have been so concerned about their regulatory prerogatives that they have been willing to sacrifice what they know is good for consumers in order to protect their fiefdoms.

Until regulators start advocating for auto insurance reforms that provide more choice, lower costs and better compensation — such as the federal Auto Choice Reform Act or similar legislation on the state level — they will be merely rearranging the deck chairs on the Titanic.

"Regulators as well as trial lawyers, defense attorneys and many insurers are responsible for not giving consumers what they need and deserve. Each group is more concerned with protecting its own turf rather than the welfare of motorists."

Mr. Kinzler is President of the Coalition for Auto-Insurance Reform, based in Alexandria, Virginia.

Sean Mooney

Is state insurance regulation dead?

State regulation of insurance is not dead, but it will be severely challenged in the new millenium. The key challenge to state regulation is the increased potential for international transactions on the Internet. How should the state regulatory system respond to this challenge? The issue here is not that of state versus federal regulation. In the borderless world of the Internet, the federal government is almost as lacking as any state in its ability to regulate directly a non-United States insurance vendor.

Before turning to solutions, perhaps it is worth asking what is the purpose of regulation in this context. The general purpose of state regulation for personal lines insurance would appear to be consumer protection. Economists would argue that consumer protection can be achieved in the private sector, without the assistance of government regulators. While this is probably true in theory, in the current world consumers expect that the insolvency of an insurer will not hurt them. They have been conditioned to believe that government authorities are looking out for them. That is why there are guarantee funds in all 50 states and why there are few instances where consumers are hurt by the collapse of an insurer.

It would appear to be unreasonable to expect states to guarantee protection to policyholders that do business on the Internet with insurers outside the United States. This would be an obvious prescription for disaster, as United States regulators have minimal ability to discipline potentially unscrupulous foreign operators. It would therefore appear that the key role for state regulators in this area would have to be in the area of consumer information. The key messages to consumers should be:

1) If you purchase insurance directly on the net from a foreign company, you lose guarantee fund protection. You are on your own. You could lose your life savings in the case of life insurance. You may end up paying your own claims in the case of auto or home insurance.

2) Before you purchase, check out the financial status of the foreign insurer through reviewing claims paying ratings and other sources.

State regulators could enlist Internet companies, including key portals, Internet Service Providers (ISPs), and individual sites to publicize these messages.

While over time there may evolve a supranational licensing and regulatory system for insurers around the globe, in the interim the best role for regulators for cyber space transactions will probably be in getting better information to consumers on the risks they face if they purchase insurance on the Internet.

Sean F. Mooney, Ph.D, is Research Director and Economist for Guy Carpenter & Company, Inc., and previously served as Senior Vice President and Economist at the Insurance Information Institute. He authors a monthly column on industry issues for the *National Underwriter.*

George Nichols

My thoughts on the future of insurance regulation truly came into focus one Friday afternoon as I sat with Tina and Terry Justice, a rural Kentucky family who were offered $23,000 by their insurer after suffering nearly $100,000 in fire losses to their home. As I sat in the Justices' newly rebuilt kitchen in Campbellsburg, I learned more from this young mother of two grade-school children than I could from any big city banker, Wall Street investor or government bureaucrat.

The Justices had lost everything in an August 1998 fire that struck just one week after their children, Christopher and Courtney, had purchased their new school clothes and supplies. I listened as Tina emotionally recounted how upset Christopher was that his Dukes of Hazzard cards were gone, how firefighters had discarded Courtney's charred Barbie doll, and how their fish had not survived the blaze.

These are the real people we serve. Tina is a young lady who found the resolve to stand up and fight for what she was owed. She and Terry had paid premiums every year on their home since they purchased it a decade ago. Now their insurer was turning its back on them and they knew it was unfair.

Tina said she had very low expectations when she first called our Department of Insurance. Jack Wiley, the Consumer Protection employee who happened to answer her first phone call, remained on the case until the final check was delivered. Jack made more than 20 phone calls during that time and helped boost Tina's morale when Christmas approached and the battle waged on.

Second only to the fire was the ordeal Tina endured with her insurance company. She could not even get a basic living allowance for her family. Once Jack was on the case, a $2,500 check went out immediately and ultimately we got the Justices a settlement close to $100,000 after an endurance contest that went far too long.

The Justices are not Wall Street investors or traders. It is not a big deal to them whether banks sell insurance or the extent to which mega-mergers will affect the future of financial services. But all their financial wealth was on the line when that heating pad shorted out and caught fire.

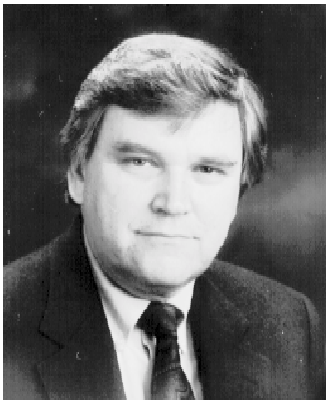
When folks like the Justices call, the Kentucky Department of Insurance is there. We know where Campbellsburg, Kentucky, is and we are prepared to help. I know all states feel the same way about their consumers. I cannot imagine the Federal Reserve or the Office of Comptroller making such an effort. Inside the Washington Beltway, they might have trouble finding Campbellsburg on the map.

George Nichols III is Kentucky's Commissioner of Insurance and the current Vice President of the National Association of Insurance Commissioners.

Nationwide, all of our states' insurance departments are handling nearly four million complaints and inquiries each year. Moreover, approximately 10,000 people across the country are devoting their professional attention to insurance regulation. Thus, it would take a new federal bureaucracy nearly the size of the Department of Housing and Urban Development (13,072 employees) to appropriately serve this country's insurance consumers.

We already have the insurance regulators in place who know this business and, more importantly, are closest to the consumer.

John Reiersen



State insurance regulation is not dead, but unless regulators and the industry take strong action, we may be viewing the beginning of the end.

Many challenges exist to state regulation especially in light of financial modernization, globalization and the Internet. While these are the most commonly discussed threats to state regulation, I am more concerned with the outsourcing of the examination function and the politicization of regulatory decisions.

Is state insurance regulation dead?

I was an insurance regulator for 25 years and for the past 10 years I have served as President of a medium-sized property and casualty insurer. I have significant experience as an examiner and as the subject of examinations. All Insurance Departments want to do a good job, but I believe most are hampered by a shortage of examiners and inadequately trained staff. Good insurance regulation demands an adequate supply of well-trained, independent insurance examiners.

I have the following concerns:

1. Many Departments today are understaffed with very little in the way of systems and actuarial resources. This has forced states, in an effort to keep their accreditation status, to hire CPA, actuarial and other consulting firms to do a significant part of the examination. The use of outside consultants to do the work of examiners prevents the proper training of examiners since the primary way to learn how to examine insurance companies is to get your feet in the fire.

I question the independence of some CPA and consulting firms in performing financial and market conduct examinations. The result is also a very expensive audit, the costs of which must be borne by the insurer. Rather than hire and train an examiner staff, some states find it easier to hire a consultant and then pass the costs of such consultants on to the carrier.

When I examined insurers, state-employed examiners performed all aspects of the examination. I believe an examiner's independence is paramount and the best regulatory system is the one that utilizes well-trained, experienced Insurance Department staff. The result is consistent and knowledgeable findings at a significantly lower cost to the regulated entity. Too many cooks spoil the brew.

2. Another disturbing trend is the role that politics plays in making regulatory decisions and policy. I am proud to say that during my tenure as an examiner, no decision or finding of mine was overruled as a result of politics. Today I observe that throughout the country politics often drives regulatory decisions. Regulation, to be effective, must be consistently and effectively applied. All insurers ask is a level playing field with regulation focused on removing the bad actors. Elected commissioners, in an effort to get re-elected, sometimes are swayed by the desire to please voters rather than regulate in a manner

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Reiersen

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consistent with the law.

Regulators are concerned with the solvency of insurers, yet they refuse to grant necessary rate increases, forcing insurers to either flee the state or go out of business. Today the industry is engaged in suicidal competition, which will result in the demise of many insurers due to merger, consolidation or liquidation. When will regulators start enforcing the statute that requires rates to be adequate? Why do we need rate regulation if unfettered competition will rule the rate level? Even worse is the practice of rate suppression practiced by too many regulators on personal lines rate filings.

Unfortunately, I fear that independence, adequate resources and adequate training for insurance regulators will only come after we suffer a significant insurance crisis and then the answer might be federal regulation.

Insurance regulators should avail themselves of all educational opportunities available through IRES, SOFE and the CPCU Society. Don't let CPA firms usurp your legitimate function. Your acquired expertise will encourage you to insist on consistent and focused regulation. Available resources should be focused and targeted on material items and on problem insurers with financial or market conduct problems.

John Reiersen worked as a New York insurance regulator for over 25 years and was a founding director of the Insurance Regulatory Examiners Society. In the early- to mid-1970s, he helped develop and design New York's no-fault automobile insurance system. Mr. Reiersen is president of the Eagle Insurance Company, located in Long Island, New York.

C.E. News

Updates and other tidbits from the National IRES Continuing Education program. The C.E. program is for persons holding AIE and CIE designations.

DID YOU MISS THE CE DEADLINE?

Designee holders who missed the Oct. 1 deadline for reporting required continuing education credits during the annual compliance period, Sept. 1, 1998 to Sept. 1, 1999 will soon be receiving notices from the IRES CE Office that IRES will no longer recognize their designation.

To be automatically reinstated, designee holders must certify all past CE hours and pay a $60.00 reinstatement fee. Those who filed extensions prior to the deadline have one year to complete the required CE hours.

If insufficient CE hours were earned during the compliance period, a written appeal for reinstatement must be made in writing to the Accreditation & Ethics Committee in care of the IRES CE Office.

NEXT DEADLINE IS OCT. 1, 2000

The new 15 hour annual CE program is now in effect. It began Sept. 1, 1999 and ends Sept. 1, 2000. An extension may be requested in writing prior to September 1 of each year to complete and report the 15 hours required for that year. Current year hours will continue to accrue. A member may not be more than 15 hours in arrears each September 1.

All CE credit for the current compliance period must be earned in the current reporting year. (9/1/99-9/1/2000). **No carryover of credits from the previous year's compliance period will apply.**

More questions? Call us at 913-768-NICE

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Angela Ford

Is state insurance regulation dead?

If I had to answer this question, my response would be “Definitely Not!” The term “dead” would imply that state regulators have closed shop and are simply waiting for “Out Of Business” signs to be placed on our offices. The current challenges presented to state regulation should be viewed as a wake-up call for state regulation.

Globalization, financial integration and sales on the Internet are just a few of the challenges to state regulation. Much remains to be seen with globalization and financial integration due to possible changes in state and federal laws. As such, sales on the Internet are a current concern for all regulators.

Regulators are accustomed to some type of paper documentation to evidence an insurance transaction (approved application and marketing materials, licensed agent or broker, etc.) This documentation provides the regulator with a degree of comfort regarding the insurance product and the seller of that product. With insurance sales on the Internet, regulators are sometimes the last to learn of a website’s existence.

As websites are developed, licensing issues have arisen. Most states require the selling of insurance through a licensed agent or broker. With the Internet, the seller may or may not be licensed. Additionally, there is no guarantee that the product being sold is a legitimate insurance product. To compound this problem, some websites allow payment of the purchased product to be conducted via the Internet.

If the product offered on the website is backed by a properly licensed producer and insurer, minimal concerns should exist. Some questions may, however, arise due to consumer confusion. When a product is purchased on the Internet when is the coverage effective? Does the consumer assume that coverage is in effect when payment is made? What type of documentation does the consumer receive to verify “proof of purchase?” Is the consumer aware that additional underwriting (inclusive of credit checks) will occur and that the pricing arrangement may change.

As we ponder Internet sales, quite a few questions come to mind. Most of them can be addressed by establishing definitive parameters for insurance sales on the Internet.

There are some that believe banks and financial institutions are better equipped to market products on the Internet as insurance companies may be reluctant to change current distribution channels. Some companies may think that their current distributions have worked for years and that a change to include the Internet may not be cost effective (website development, producer disenchantment, etc.) Others believe marketing on the Internet is here to stay and that one needs to find the correct methodologies to venture forth in this new arena. If I were a betting person, I’d place money on “It’s Here To Stay!”

The primary challenge to regulators is to develop consumer safeguards to address issues presented by the sale of insurance on the Internet. This is an opportune time for regulators to demonstrate our primary purpose — protection of the consumer.

Angela K. Ford is president of the Insurance Regulatory Examiners Society and is a senior deputy commissioner at the North Carolina Department of Insurance.

REGULATORY ROUNDUP

EDITOR'S NOTE: *This month's Roundup focuses on recent federal v. state developments around the country.*

by Dee Dee Gowan

COLORADO — Federal Preemption of State Benefit Forms for Medicare Plans

The Colorado Division of Insurance issued a new bulletin to inform carriers selling Medicare plans that they are no longer subject to a Colorado statute and regulation requiring the use of standardized forms to describe health plan benefits. The Health Care Financing Administration recently issued a letter pre-empting state authority with respect to the application of state standardized description form laws for Medicare managed-care plans. Instead, HCFA now requires Medicare insurers to use a federal standard health benefit description form. If you have any questions, you can call Barbara Yondorf, Colorado Division of Insurance, (303) 894–7499, ext 308. For more information, see *CO Bulletin 5-99 (July 16, 1999).*

ILLINOIS — U.S. Supreme Court to Decide Whether HMO Financial Structure Violates ERISA The United States Supreme Court has agreed to hear a case involving an Illinios HMO and its cost-containment strategy, which links a doctor's compensation to his ability to hold down health care costs. Herdrich v. Pegram, 154 F.3d 362 (7th Cir. 1998), *cert. granted*, 67 U.S.L.W. 3758 (U.S. Sept. 28, 1999) (NO. 98-1949). The Supreme Court should hear the case in January and is expected to issue a decision this spring on (1) whether the HMO and its doctors had a fiduciary duty under the Employee Retirement Income Security Act to act in the patients' best interest, and (2) whether by rewarding doctors for holding down costs, the HMO may have violated this duty under ERISA by placing the doctors' interest in conflict with the interests of patients.

KENTUCKY — Exclusive Jurisdiction Over Insolvency Matters Does Not Apply to Breach of Contract Actions

A federal district court in Kentucky ruled that it had jurisdiction to hear a breach of contract action brought by the Kentucky Insurance Commissioner, acting as liquidator for an insolvent insurer, against a second insurer. Nichols v. Vesta Fire Ins. Corp., 56 F.Supp.2d 778, 780-81 (E.D. Ky. 1999). The Kentucky statute granting the state court exclusive jurisdiction to hear cases relating to delinquency proceedings did not deprive the federal court of proper jurisdiction to hear the breach of contract action. The court explained that just because the breach of contract action happens to involve an insolvent insurer is not enough to invoke the provisions relating to state court exclusivity. Rather, reverse-preemption is only an issue if the case involves delinquency proceedings or the distribution of the insolvent insurer's assets to creditors.

NEW JERSEY — Federal Court Allows HMO's To Be Sued in State Court

The United States Third Circuit Court of Appeals has ruled that an HMO may be sued in state court for failing to provide quality health care when the HMO has assumed the role of health care provider in addition to its role as health care administrator. In re U.S. Healthcare, Inc., 1999 WL 728474, *6-12 (3rd Cir. 1999). In this case, a newborn baby died one day after being discharged under the HMO's 24-hour pre-certified discharge policy and after the HMO failed to provide in-home nursing care as requested. The parents brought suit against their HMO in a New Jersey state court for failing to properly treat their baby. The HMO removed the case to federal court and argued that the claim was based on a denial of benefits and, therefore, was governed by and completely pre-empted by the Employee Retirement Income Security Act. The court disagreed and explained that the basis for the claims related to the quality of care received rather than a denial of benefits.

TEXAS — Life Insurers Need to Identify Viatical "Cleansheeting" Practices The Texas Department of Insurance issued a new bulletin to address concerns that some life insurance agents, viatical settlement brokers and viatical settlement companies are "cleansheeting" or fraudulently selling life insurance policies for the sole purpose of viaticating the policies. In a legal viatical settlement, a terminally ill person sells his life insurance policy for a discounted value to a viatical settlement company who then markets the policy to investors. Recently, the Texas Department has learned that some agents and brokers may be selling life insurance policies to ill consumers who then provide false or misleading answers on the application regarding their health and medical history to obtain the policy solely for the purpose of viaticating the policy. The new bulletin explains various patterns of cleansheeting and recommends that insurers begin to identify these patterns as soon as possible to protect their financial integrity. If you have questions, contact Beth Hill, Texas Insurance Department, at *beth_hill@tdi.state.tx.us* or call her at (512) 322-3406. For more information, see *TX Bulletin B-0038-99 (July 12, 1999)*.

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THE REGULATOR®

Published by the
Insurance Regulatory Examiners Society
130 N. Cherry, Suite 202, Olathe, Kansas 66061

www.go-ires.org

Is state insurance regulation dead?

A REGULATOR SPECIAL REPORT

BULLETIN BOARD

√ **Welcome new IRES members:** Mary T. Dampman, Kentucky; Douglas R. Hartman, Arkansas; Kathleen Kalk, Oregon; Hernan C. Macapanban, Florida; Richard Zafuto, Oregon.

√ We are sorry to report that IRES member Donald R. Walker, CIE, financial analyst for the Georgia Insurance Department, passed away Sept. 17.

√ Year 2000 member dues notices will be mailed to IRES members in late December. Please notify us at once if you have recently changed your address.

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