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November 5, 2010

The Honorable Timothy F. Geithner
Department of the Treasury
1500 Pennsylvania Avenue
Washington, D.C. 20220

Re: Advance Notice of Proposed Rulemaking Regarding Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies; Docket Number FSOC-2010-0001

Dear Secretary Geithner:

The Reinsurance Association of America ("RAA") appreciates the opportunity to provide comments in response to the Financial Stability Oversight Council's ("the FSOC" or "the Council") Advanced Notice of Proposed Rulemaking ("ANPR") Regarding Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies.

The RAA is the leading trade association of property and casualty reinsurers and life reinsurers doing business in the United States. RAA membership is diverse, including reinsurance underwriters and intermediaries licensed in the U.S. and those that conduct business on a cross border basis. The RAA represents its members before state, federal and international bodies.

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("the DFA" or "the Act") sets forth the standard for designating a nonbank financial company. This standard is a high one and should be complied with: for a nonbank financial company to be subject to heightened prudential standards and Federal Reserve Board supervision, the FSOC, must find that the material financial stress, or the ongoing activities of the company, could pose a threat to the financial stability of the United States.

As an initial matter, when FSOC is making a determination under the Act, the activities which the company is engaged in should be of paramount importance in defining any potential threat to the financial stability of the United States. A March 2010 report by The Geneva Association[1], entitled, "Systemic Risk in Insurance: An analysis of insurance and financial stability (attached) ("the Geneva Report"), is instructive in differentiating the significant differences between banks and (re)insurers and why (re)insurers do not pose a systemic risk.

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[1] The Geneva Association (The International Association for the Study of Insurance Economics) is the leading international insurance "think tank" for strategically important insurance and risk management issues. It is a non-profit organization comprised of the CEOs from the world's top (re)insurance companies.

The report importantly points out that banks and insurers played very different roles in the recent financial crisis; namely, banks, not insurers, were the source of the crisis and were more heavily affected. Banks received over $1 trillion in direct State support as opposed to $10 billion for insurers (excluding those with large quasi-banking operations). The few insurers that experienced serious difficulties did so because of these banking activities (financial guarantees, CDS writing and trading), not because of their insurance operations.

The RAA supports the submissions of the American Council of Life Insurers (ACLI) and the Property Casualty Insurers Association of America (PCI) on FSOC for this ANPR. Reinsurance is very similar to insurance in its structure and effect on the economy and much of their submissions is applicable to our industry. Thus, this short letter is meant to explain the few ways in which reinsurers differ from primary insurers.

Reinsurance plays a critical role in the economy and particularly in the insurance marketplace. It is a risk management tool for insurance companies to reduce the volatility in their portfolios and improve their financial performance and security. It is widely recognized that reinsurance performs at least four primary functions in the marketplace: to limit liability on specific risks; to stabilize loss experience; to provide transfer for insurers of major natural and man-made catastrophe risk; and to increase insurance capacity. Hence, reinsurance provides another means for insurers to manage and balance their risks. It diversifies their risk portfolio by allowing them to transfer to the reinsurer risks in which the insurer may have become overly concentrated for its business plan. Reinsurers are able to do this because of their own highly diversified portfolio of risks. Large reinsurers tend to be geographically diversified – typhoons in Asia are not correlated with hurricanes in the Gulf of Mexico. Reinsurers are also diversified by product. Mortality, property and casualty risks are, at best, minimally correlated risks.

Reinsurers provide stability, particularly during times of financial stress. Reinsurers have assisted in the recovery from every major US catastrophe over the past century. By way of example, 60% of the losses related to the events of September 11 were absorbed by the global reinsurance industry, and in 2005, 61% of Hurricanes Katrina, Rita and Wilma losses were ultimately borne by reinsurers.

Despite the important role of reinsurance, the failure of even a very large reinsurer is unlikely to result in systemic risk[2]. A 2006 Group of Thirty Report on Reinsurance and International Financial Markets[3] concluded that there is no evidence that the failure of an insurance or reinsurance company in the past has given rise to a significant risk of systemic risk. The report found that even a loss of some 20% of global reinsurance capacity (which would be 35 times greater than the sum of all reinsurance failures from 1980 to 2003) would be unlikely to cause widespread insolvencies in the primary industry and would have only a limited effect on the financial system and real economy generally.

In 2010, the industry's lack of systemic risk remains the case. The Financial Stability Board has utilized three criteria to assess the systemic risk presented by an institution: size, interconnectedness

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[2] Swiss Reinsurance Company, "Striking the right balance: Insurance and systemic risk regulation", 2010

[3] The Group of Thirty, established in 1978, is a private, nonprofit, international body composed of very senior representatives of the private and public sectors and academia. The Group's stated aim is to deepen understanding of international economic and financial issues, to explore the international repercussions of decisions taken in the public and private sectors, and to examine the choices available to market practitioners and policymakers.

and substitutability. The International Association of Insurance Supervisors (IAIS) has added time (the speed of loss transmission to third parties) as an additional criterion. Importantly, these criteria focus not on the institution but rather on its activities. When these criteria are applied to the core activities of reinsurers (such as investment management, liability origination, risk transfer and capital management), it is clear that these activities do not pose a systemic risk for one or more the following reasons:

- Most reinsurers are relatively small as compared to other financial institutions, so their limited size means there would not be disruptive effects on financial markets. The larger reinsurers have diversified portfolios, both geographically and by product risk. Reinsurers do not increase risk by leveraging. Instead, they assume a portion of insurers' risk, thus spreading it over a wider range of corporate entities. This serves to stabilize the insurance industry a as well as the financial system as a whole.
- Reinsurers, like insurers but unlike banks, pay out claims over a long period of time. Claims are not immediately "callable" like deposits at a bank. Instead, after an insured event occurs, the claims process may take place over a number of years (e.g., a claim involving a long medical treatment or a long payout of income support). This longer payout process also allows for an orderly wind-up, in the unlikely event of an insolvency.
- Though reinsurers are connected to the insurance industry and the companies within it, this interconnectedness is unlikely to increase contagion risk. Contagion risk is increased when leverage is employed; reinsurers on the other hand, are in the business of risk transfer which serves to spread risk throughout the world thereby providing a stabilizing effect.
- There is also a great deal of substitutability in the reinsurance sector. Immediately following any major event in which reinsurers suffer heavy losses, capital flows in to the industry. This can take many forms – newly raised equity capital, start-up companies, and various financial structures that obtain non-equity capital from institutional investors.

As noted in the Geneva Association report, current and already approved (re)insurance regulatory regimes adequately address insurance activities. The remaining issue is whether existing regulation adequately mitigates potential systemic risk from these non-core activities or whether it needs to be supplemented. This report concludes that principle-based group supervision applied to all entities within an insurance group (both regulated and non-regulated), supported by sound industry risk management practices, will mitigate potential systemic risk related to those activities. The report cautions against the addition of special burdens on specific institutions because this could distort the insurance market by skewing pricing, reducing aggregate market risk-bearing capacity, drawing supervisors' attention away from risky activities going on elsewhere and creating moral hazards in these "too big to fail" institutions. The report also warns that "the consequences of getting systemic risk reforms wrong would not only be severely damaging to the insurance industry but to the economy as well."

We appreciate the opportunity to comment and are available to discuss these issues further.

Sincerely yours,

Tracey Laws
Sr. V.P. & General Counsel

Attachments