UPDATE: THE IMPLEMENTATION OF THE DODD-FRANK ACT AS IT MAY RELATE TO INSURANCE INTERESTS

by

Roland C. Goss

March 7, 2011

The implementation of the Dodd-Frank Act ("DFA") has continued in several areas of interest to those in the insurance sector. Although final rules have yet to be adopted, studies have been published and preliminary rulemaking has occurred in a number of the areas covered by our prior DFA posts in ReinsuranceFocus.com.

Concerns have been raised over the lack of consideration of insurance perspectives in the implementation of the DFA. There are to be three persons with insurance expertise involved in the implementation of the DFA: (1) the Director of the Federal Insurance Office (to be appointed by the Treasury Secretary); (2) a voting member of the Financial Stability Oversight Council ("FSOC") with insurance expertise (to be appointed by the President and confirmed by the Senate); and (3) a non-voting member of the FSOC, to be a state insurance commissioner, selected by all state insurance commissioners. So far, the only one of these three positions to be filled is that of the non-voting member of the FSOC. The NAIC appointed the current Missouri Insurance Director, John Huff, to that position. According to news reports, however, the Treasury Department has taken the position that Director Huff represents only the State of Missouri, and has blocked him from sharing confidential information with other insurance regulators.

The NAIC and several members of both the House and the Senate in leadership positions on financial services committees have expressed concern that the FSOC is about to make important decisions regarding systemic risk regulation without the input of the insurance experts contemplated by the DFA, and have asked that the FSOC defer action until the insurance experts are appointed. Treasury Secretary Geithner chairs the FSOC, which is located within the Treasury Department. There has been no acknowledgement of this issue yet by Secretary Geithner, the Treasury Department or the FSOC.

Following is a summary of activities by various federal agencies and other DFA implementation activities which have occurred over the past couple of months.

- Financial Stability Oversight Council ("FSOC")
    - The FSOC has been engaged in rulemaking that identifies thirteen criteria and the processes to be used for the FSOC's designation of nonbank

financial companies for enhanced prudential regulation under the DFA.[1] This is largely a repetition of factors contained in the DFA, which include the extent to which a company is regulated, a factor which should be particularly relevant in the consideration of insurance companies.

- Media stories have referred to a FSOC staff study on prudential regulation standards which reportedly includes vague statements such that the failure of a large insurance company could "reduce overall investor sentiment" and affect "the general conduct of economic activity." Such statements may suggest that insurance companies will not be exempted from enhanced prudential regulation. Without addressing its substance, Treasury Secretary Geithner has described the report as an outdated draft, with a final version expected to be released this spring.

- The FSOC has published a study and recommendations relating to the implementation of the Volcker Rule, which proposes an exception for certain hedging investments made by insurance companies for their own account.[2]

- The FSOC has published a study and recommendations regarding the implementation of the merger and consolidation provisions of section 622 of the DFA based upon concentration limits on large financial companies.[3]

- Federal Reserve

  - The Fed has issued a proposal outlining the types of companies that might be considered for enhanced prudential regulation. Insurance companies with $50 billion or more in combined assets may qualify. The approach appears to be not to exclude potentially significant companies on definitional grounds. There is a comment period open on this proposal until March 30, 2011.[4]

---

1 This proposed rule is available at http://www.treasury.gov/initiatives/Documents/Nonbank%20NPR%20final%2001%2013%2011%20formatted%20for%20FR.pdf.

2 This study is available at http://www.treasury.gov/initiatives/Documents/Volcker%20sec%20%20619%20study%20final%201%2018%2011%20rg.pdf.

3 This study is available at http://www.treasury.gov/initiatives/Documents/Study%20on%20Concentration%20Limits%20on%20Large%20Fims%2001-17-11.pdf.

4 This proposal rule is available at http://edocket.access.gpo.gov/2011/pdf/2011-2978.pdf.

  - The Fed has a web page listing its DFA-related activities.[5]

- Federal Deposit Insurance Corporation ("FDIC")

  - The FDIC has issued what it terms an interim final rule regarding the DFA's orderly liquidation process which recognizes the statutory provision that insurance companies are to be liquidated under state insurance insolvency laws. The rule provides that non-insurance subsidiaries of insurance companies and insurance holding companies may be liquidated by the FDIC, and that such liquidation may result in liens on insurance company assets.[6]

  - The FDIC published a study on the Volcker Rule, which is set for rulemaking by the FDIC in April-July 2011.[7]

- Commodity Futures Trading Commission ("CFTC") and Securities Exchange Commission ("SEC")

  - The CFTC and the SEC have been engaged in rulemaking on a broad range of DFA-related issues, including the implementation of the swap provisions of the DFA. Insurance companies and other end users of swaps have lobbied for exclusion from these provisions. Although rulemaking to date has tended to exclude end users from some of the swap provisions, such as clearing requirements, the most important part of this rulemaking for insurance interests probably will relate to the definitional sections of the swap provisions. The rulemaking regarding the definitions is sequenced to occur after most of the other rulemaking, and it is not possible to predict the likely outcome of such rulemaking.

  - The CFTC and the SEC have been engaged in rulemaking on many other DFA-related issues of less potential interest to the insurance sector. Both agencies maintain web sites with additional information.[8]

---

[5] This web page may be found at http://www.federalreserve.gov/generalinfo/foia/dfproposals.cfm.

[6] A copy of this rule is available at http://www.fdic.gov/regulations/laws/federal/2011/11finalJan25.pdf.

[7] The FDIC's completed DFA-related activities and future DFA-related activities are described at http://www.fdic.gov/regulations/reform/initiatives.html.

[8] For information on the CFTC's DFA-related activities go to http://www.cftc.gov/LawRegulation/DoddFrankAct/index.htm. Information on the SEC's DFA-related activities may be found at http://www.sec.gov/spotlight/dodd-frank.shtml.

- Nonadmitted and Reinsurance Reform Act ("NRRA")

  - The surplus lines and reinsurance provisions of the DFA, contained in the NRRA (Title V, Subtitle B of the DFA), are scheduled to become effective in July of 2011. Many of the issues identified in the NRRA were left to state regulation. In particular, the NRRA encourages states to enact laws and suggests an interstate compact regarding the collection of surplus lines premium taxes. The National Association of Insurance Commissioners ("NAIC") and the National Conference of State Legislatures ("NCOIL") have adopted different premium tax model acts for consideration by states. The NCOIL model has been endorsed by the Council of State Governments and the National Conference of State Legislatures. While the NAIC version deals exclusively with premium tax issues, the NCOIL version addresses issues beyond premium taxes, including issues relating to companies, brokers and insurance placement. Bills pending in the Florida (HB 1127; SB 1816) and West Virginia (HB 2963; SB 435) legislatures follow the NAIC model, while bills pending in the Indiana (SB 578), Kansas (SB 178; SB 206), Kentucky (HB 167), Maryland (HB 911; SB 964), New Mexico (SB 250), North Dakota (HB 1123), Rhode Island (HB 5110; SB 88), Tennessee (HB 966; SB 1025), Texas (HB 1535) and Vermont (HB 164; SB 36) legislatures follow the NCOIL model. Bills have been introduced in the Connecticut (HB 6363; SB 50; SB 975) legislature following both the NAIC and the NCOIL models, and Arizona (HB 2112), Hawaii (HB 1052; SB 1279), New Hampshire (HB 424), Oklahoma (HB 2073; SB 959), South Dakota (HB 1030 – adopted and signed by the governor) and Utah (HB 316) have bills pending or adopted authorizing the insurance commissioner to enter into a compact or multistate agreement without specifying either the NAIC or the NCOIL models. It remains to be seen whether there will be material differences in the surplus lines premium tax provisions adopted by the states, and if so, the potential impact of any such differences.

  - Some industry groups have asked that the effective date of these provisions be postponed to allow the states additional time to address these issues.

- Federal Insurance Office ("FIO")

  - As mentioned above, the FIO, which was established by the DFA, is still without a director.

- o There has been little if any publicly noticeable progress in the establishment of the FIO.

****

This article does not constitute legal or other professional advice or service by JORDEN BURT LLP and/or its attorneys.

Roland C. Goss is a partner with Jorden Burt LLP, resident in its Washington, DC office, and the blogmaster of Jorden Burt's reinsurance and arbitration blog, www.reinsurancefocus.com.