The Honorable Christopher Dodd
Chairman
Senate Banking Committee
534 Dirksen Senate Office Building
Washington, DC 20515

The Honorable Barney Frank
Chairman
House Financial Services Committee
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Richard Shelby
Ranking Member
Senate Banking Committee
534 Dirksen Senate Office Building
Washington, DC 20515

The Honorable Spencer Bachus
Ranking Member
House Financial Services Committee
2129 Rayburn House Office Building
Washington, DC 20515

April 9, 2009

Dear Chairman Dodd, Chairman Frank, Ranking Member Shelby, and Ranking Member Bachus:

You have recently received a letter signed by a number of state governors requesting that you reject legislation that would provide for federal oversight of insurance companies. We agree with the governors' request that Congress "thoroughly review" the prospect of certain types of federal oversight, but wish to raise some questions about some specific claims made in the letter. We address three particular claims in order.

Claim: "The state regulatory system… has remained sound despite the catastrophic disruptions we have witnessed as a result of failed federal oversight and regulation."

Analysis: The soundness of the state regulatory system remains unproven. One state, New York—whose governor is *not* among the signers of the letter you received—authorized AIG to raid its property and casualty subsidiaries for funds when the company nearly collapsed last fall. Recent reports, likewise, indicate that many of AIG's other state-regulated subsidiaries have financial problems of their own. The

state-level insurance system, in short, has not avoided the problems that have afflicted other financial sectors.

Claim: "States. . . often lead the way with regard to reform and innovation and this is true of insurance regulation."

Analysis: Obviously, states sometimes innovate in ways that the federal government does not or cannot. But the state insurance regulatory system has not served the interests of innovators or consumers well. No fundamentally new personal lines insurance products have become available since modern all-perils homeowners' insurance first became available in 1959. Promising innovations like pay-per-mile automobile insurance, likewise, have found themselves stymied by state-by-state regulatory hurdles. Americans today have different types of bank accounts, mortgages, and investment opportunities than their ancestors. The personal lines property and casualty insurance products sold today, however, are fundamentally the same as those sold in the early 1960s.

Claim: "Under the Treasury model, states stand to lose revenue generated from current fees and assessments. The potential outcome of such actions could further endanger our ability to provide critical health care, education, and unemployment resources to citizens of our respective states."

Analysis: Quite simply, the governors have it wrong. The proposed federal legislation currently on the table and the Bush administration Treasury proposal (which, in any case, isn't something that the Obama administration appears likely to enact without changes) would let states keep the premium taxes assessed on insurance companies. These taxes as well as general business taxes (corporate income taxes, property taxes, business license fees) are the ones that support "health care, education, and unemployment" programs. And, under all proposals, insurers would still have to pay them. Under the National Insurance Consumer Protection Act—the proposed national regulatory bill—states would also continue to collect the "assessments" levied against companies for insolvencies and support of state-level residual markets. The states would only lose licensing fee income which, in almost all cases, simply supports the cost of the systems that oversee insurance rates and monitor insurance agents' licenses. In short, states will lose only a trivial amount of revenue under the proposals and the revenue they do lose pays only for activities that they will no longer have to perform. It's extremely unlikely that any state will see any significant impact to its revenue as a result of any proposal.

In short, many of the key claims that the governors' make lack a sound evidentiary basis. Many factors ought to play into the support or opposition to proposed federal regulation and the governors do make many legitimate points. But a truly thorough review requires additional analysis and oversight.

Yours truly,

Eli Lehrer, Senior Fellow: The Competitive Enterprise Institute

Wayne Brough, Vice President and Chief Economist: FreedomWorks

Steve Pociask, Chief Economist: American Consumer Institute