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1001 Connecticut Ave NW • Suite 1250 • Washington, DC 20036
202.331.1010 • www.cei.org
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Toward a National Market for Insurance

How an Office of Insurance Information Can Help Us Get There

By Eli Lehrer*

As Congress considers financial proposals involving everything from mortgage reform to credit card regulation, it should seek to improve America's international competitiveness by liberalizing property and casualty insurance. A proposal recently introduced in Congress, the Insurance Information Act of 2008 (H.R. 5840), would create a new Office of Insurance Information (OII), which, if enacted as a stopgap measure, and not as a policy end point, would begin the process of removing impediments for U.S. firms to operate in a liberalized national—and ultimately international—environment.

The creation of this office would represent an incremental—though temporary—step in efforts to open America's insurance markets to greater competition and innovation. This paper briefly outlines the current scope of insurance regulation, describes the functions of the proposed office, and shows how the resulting economic flexibility would improve America's international competitiveness as financial services become increasingly globalized.

Current Scope of Regulation. America's property and casualty (P&C) insurance industry represents nearly 45 percent of the world's P&C market, provides almost 700,000 jobs, and represents about 4 percent of the country's gross domestic product.[1] Unlike other nationwide industries, which are federally regulated, all insurance-specific regulation takes place at the state level (the District of Columbia and all U.S. territories each also have their own regulator).[2]

Insurance regulation varies greatly across the country, and states enjoy a great deal of latitude in regulation. The problem with the current system is not a lack of regulation, but an imbalance between the competitive disciplines of the market and the lack of any discipline on state officials. Today, companies must operate only under the regulations of states where they sell policies, while consumers can buy policies only in the states where they live.[3]

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* *Eli Lehrer is a Senior Fellow at the Competitive Enterprise Institute. He wishes to thank Ivan Osorio for his assistance with this paper.*

This reflects a lack of competition *between regulators*, which has resulted in a moribund industry that has failed to produce a single fundamentally new personal lines property and casualty product since *1959*.[4]

An Office of Insurance Information would represent a first step towards creating a degree of regulatory competition across the United States. It would not by itself create overall choice in regulation, but it would help create the conditions to get there.

How Would the Office Work? The Insurance Information Act would establish an Office of Insurance Information, within the Department of the Treasury, to serve as the federal government's main repository of expertise on insurance. It would represent federal interests in insurance regulation—largely related to international issues—and issue studies on the national insurance environment. It would not have any authority to preempt state regulation except pursuant to international agreements—a power already accorded to the federal government under the Constitution. It would not deal with health insurance.

A nine-member advisory group made up of representatives from the National Association of Insurance Commissioners (NAIC), Department of Commerce, U.S. Trade Representative, and industry and consumer groups would advise the office on an ongoing basis. However, such advice should be transparent, and opportunities to provide comment should remain open to all parties, to prevent undue influence by a small number of interested parties.

Competitiveness in a Globalized Services Market. Current insurance law places America at a relative disadvantage in the globalized services market. For American insurers, cross-border business is nearly impossible. One of the largest American international insurers has significant American business in only one personal lines category—automobile insurance—and otherwise only does business overseas and on a business-to-business basis.[5] The companies that sell the most personal lines property and casualty insurance in the United States, State Farm and Allstate, do almost no business outside of the United States and Canada.[6]

The United States has no national negotiator for international agreements on insurance. It took eight years after implementation of the North American Free Trade Agrement (NAFTA) to reach an insurance agreement with Mexico.[7] The situation is similar among World Trade Organization (WTO) members: By most accounts, China, which has a tiny property insurance market, has reaped far greater benefits from WTO membership than has the United States.[8]

The National Association of Insurance Commissioners attempts to serve as a national representative, but, as a fractious group—its members get elected or appointed to serve the interests of their states first—it often cannot reach consensus. In practice, insurance simply gets left out of many international agreements. This has resulted in a diminished international role for American insurers; a new office would create such a negotiator without encroaching on state prerogatives.

No other major developed nation lacks a national voice in international forums dealing with insurance issues. Countries with strong central governments like the United Kingdom, France, and Japan regulate insurance only at the national level.[9] Countries with federal systems like Canada and Germany offer insurers a choice between state/provincial and national regulation. In both cases, these countries have a national insurance negotiator.[10]

Data Gathering. Most well-functioning national markets have ample sources of private sector information and research. National level information about the stock market, bank interest rates, and bonds comes almost entirely from private firms like Dow Jones and bankrate.com. Several firms and organizations—most prominently A.M. Best and the Insurance Information Institute—collect information about insurance at the state level, but the current regulatory structure has prevented the development of a private market for true national insurance market information and analysis,[11] since in the current balkanized insurance environment national insurance information has very little immediate business value.

A wide range of property and casualty insurance issues—the creation of catastrophe funds, optional federal chartering, federal wind insurance, mortgage insurance, and bond insurance—will come before Congress in the next few years. The administration and Congress need a good, reliable source of information and expertise to inform the debate. Ideally, private sources should provide this information, but given the fragmented nature of the national insurance market, there is simply no profitable incentive to provide that information.

However, an Office of Insurance Information should ultimately be only a stopgap measure until further reform can allow for the emergence of a truly national market. An Optional Federal Charter, by allowing some insurers to opt for a new federal regulator,[12] would very quickly create demand for national insurance information from those federally chartered insurers. Once this is achieved, the OII should step aside to let private enterprise fulfill that new demand for national insurance information. Legislation creating an OII should include a provision folding the office upon the enactment of an OFC (the legislation currently before Congress has no such provision).

Conclusion. The creation of an Office of Insurance Information would constitute a modest, temporary, step toward creating a simpler, nationwide regulatory environment for American insurers and consumers. It would enhance American international competitiveness and provide a national repository for insurance information that does not exist today. However, it should be temporary; legislation creating an OII should sunset the office over time, as a newly liberalized market allows for private market institutions to provide national insurance information.

Notes

[1] Insurance Information Institute, "Top Ten Countries by Non-life and life Direct Premiums Written, 2006," http://www.iii.org/media/facts/statsbyissue/international/.

[2] Of course, general business conduct regulations apply to insurance companies the same as for all other businesses.

[3] Each new insurance product must receive at least 51 separate approvals before it can be marketed nationally. About 45 states, furthermore, set premiums for at least some insurance products. Even basic data on the industry proves difficult to come by: The statistics above—the most recent available—reflect the situation almost three years ago (thus the "about").

[4] American Association of Insurance Services, "The Homeowners Class Plan: How It Has Become Folklore," Wheaton, Illinois, 2003, p. 22.

[5] Berkshire-Hathaway sells auto insurance as GEICO.

[6] Insurance information Institute, "Top Ten Global Insurance Companies by Revenues, 2006."

[7] Constance Patterson, "Insurance Groups Voice NAFTA Concerns," *Insurance Journal,* October 30, 2000.

[8] J. Tyler Leverty, Yijia Lin, and Hao Zhou, "WTO and the Chinese Insurance Industry," April 7, 2008, Working Paper Series, Social Science Research Network, http://ssrn.com/abstract=1016867

[9] Financial Services Authority (UK), "What We Do," http://www.fsa.gov.uk/Pages/About/What/index.shtml.

[10] Department of Finance, Canada, "Property and Casualty Insurance in Canada," http://www.fin.gc.ca/toce/1999/propertye.html. Very little regulation takes place at the federal level.
[11] To the extent any reports at all emanate from the federal government most come from a single analyst at the Congressional Research Service. Rawle O. King.
[12] See "Optional Federal Charter for Insurers; FAQ" by Eli Lehrer, *OnPoint* No. 122, Competitive Enterprise Institute, October 2, 2007, http://cei.org/pdf/6170.pdf.