



# Audit Report



OIG-15-032

FIO's Consultation Process with State Insurance Regulators Could Be Improved

May 15, 2015

Office of  
Inspector General

Department of the Treasury

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## Abbreviations and Acronyms

Dodd-Frank	Dodd-Frank Wall Street Reform and Consumer Protection Act
FIO	Federal Insurance Office
FRB	Board of Governors of the Federal Reserve System
G-SII	Global Systemically Important Insurers
IAIS	International Association of Insurance Supervisors
JAMES	Joint Audit Management Enterprise System
NAIC	National Association of Insurance Commissioners
Treasury	Department of the Treasury

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*The Department of the Treasury  
Office of Inspector General*

May 15, 2015

Michael T. McRaith  
Director, Federal Insurance Office

This report presents the results of our review of the Federal Insurance Office's (FIO) policy development and coordination on international insurance matters. We performed this review in response to the House Report 113-508 on the Financial Services and General Government Appropriations Bill, 2015. The House Report was incorporated by reference into the Consolidated and Further Continuing Appropriations Act, 2015, which was passed on December 16, 2014. The House Report included the following directive for our office:

“Insurance - Not less than 90 days from enactment of this Act, the Inspector General shall submit a report to the House and Senate Committee on Appropriations, the House Financial Services Committee, and the Senate Banking Committee on the Department's process for collecting input from state insurance commissioners and developing a consensus with the state insurance commissioners with respect to international insurance standards and if the Department's representation at international insurance supervisory organizations conforms with such a consensus.”<sup>1</sup>

Consistent with this directive and Title V, Subtitle A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), our audit objectives were to (1) identify the authority(s) and processes by which the Department of the Treasury (Treasury), through FIO, coordinated Federal efforts and developed Federal

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<sup>1</sup> In letters dated March 11, 2015, we informed the Committees that we planned to provide our report by May 15, 2015.

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policy on prudential aspects of international insurance matters, including representing the United States, as appropriate, in the International Association of Insurance Supervisors (IAIS) and (2) determine whether Treasury's activities, through FIO, are consistent with its authority(s) and whether such activities were appropriately informed by consultation with the States, including State insurance regulators. With respect to our second objective, we note that the provision in Dodd-Frank that created FIO provides that FIO is authorized to consult with the States regarding insurance matters, rather than reach a consensus among the States.

In brief, we found that FIO engaged in numerous activities to promulgate its role as the United States representative in the IAIS. For example, it represented the United States' interests in leadership and committee member roles in the IAIS, actively participated in IAIS conferences, and regularly communicated with State insurance regulators on the development of Federal policy on prudential aspects of international insurance matters. However, our interviews with State insurance regulators revealed that FIO could improve its consultative efforts. Accordingly, we are recommending that FIO continue and build on its existing consultation processes with State insurance regulators to provide more consistent communication, timely dissemination of information, consideration of solicited feedback, and increased transparency of FIO's activities relating to the IAIS.

In a written response, which is included as Appendix 2, management agreed with the recommendation. FIO will build on its existing consultation process with State insurance regulators in ways outlined in this report. We consider FIO's commitment to enhance its consultation process to be responsive to our recommendation. FIO will need to record the estimated date for completing its planned corrective actions in the Joint Audit Management Enterprise System (JAMES), Treasury's audit recommendation tracking system.

## Background

Dodd-Frank created FIO and authorized FIO to identify issues or gaps in the regulation of insurers that could contribute to a

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systemic crisis in the insurance industry or the U.S. financial system. In addition, FIO is authorized to monitor the accessibility and affordability of insurance to underserved communities, to develop Federal policy and coordinate Federal efforts on prudential aspects of international insurance matters, to represent the United States in the IAIS, and to consult with the States, including State insurance regulators, regarding insurance matters.<sup>2</sup>

Established in 1994, the IAIS is the international standard setting body responsible for developing and assisting in the implementation of principles, standards, and other supporting material for the supervision of the insurance sector. The mission of the IAIS is to promote effective and globally consistent supervision of the insurance industry to develop and maintain fair, safe, and stable insurance markets for the benefit and protection of policyholders and to contribute to global financial stability. Membership in the IAIS is voluntary and regulators from more than 200 jurisdictions in nearly 140 countries participate. Under Dodd-Frank, the U.S. is represented in the IAIS by FIO;<sup>3</sup> in addition, members of the IAIS include the Board of Governors of the Federal Reserve System (FRB), State insurance regulators, and, as a non-voting member, the National Association of Insurance Commissioners (NAIC).

The U.S. insurance sector is primarily regulated by the States. State insurance regulators created the NAIC in 1871 to coordinate the regulation of multistate insurers. Over time, NAIC became the U.S. insurance industry's standard-setting and regulatory support organization for the 50 States, the District of Columbia, and the five U.S. territories. State insurance regulators use the NAIC to establish standards and best practices, conduct peer reviews, coordinate regulatory oversight, and represent the collective views of State regulators domestically and internationally.

As noted above, the U.S. is represented in the IAIS by FIO. FRB represents its interests as the supervisor of insurance holding companies that own Federally chartered banks and insurance holding companies designated by the Financial Stability Oversight Council. FIO and FRB recently joined the international supervisory

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<sup>2</sup> Dodd-Frank, Title V, Section 313 (c)(1).

<sup>3</sup> Dodd-Frank, Title V, Section 313 (c)(1)(E).

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community as they became members of the IAIS in October 2011 and late 2013, respectively; the NAIC was a founding member in 1994. According to the IAIS' By-Laws, NAIC can, at any one time, designate up to a maximum of 15 of its members (State insurance regulators) who may exercise their rights to vote on IAIS matters. FIO and FRB each have one vote. These three members of the IAIS – FIO, FRB, and the NAIC – work together to share information and facilitate discussions on international matters; however, the members can and do operate independently in this multi-lateral organization. As a result, the members can have differing perspectives and desire different outcomes as international topics are scrutinized by each member.

## **Results of Audit**

### **FIO Has Processes for Conducting Activities with IAIS But Could Improve Its Consultation Process with State Insurance Regulators**

Since its establishment in July 2010, FIO engaged in numerous activities to promulgate its role as the United States representative in the IAIS. As examples, it represented the United States' interests in leadership and committee member roles in the IAIS, actively participated in IAIS conferences, and regularly communicated with State insurance regulators on the development of Federal policy on prudential aspects of international insurance matters. However, FIO can improve on its existing consultation process to establish a consistent, comprehensive consultation process with State insurance regulators.

#### **FIO's Policies and Procedures**

We asked the FIO Director what policies and procedures guide its activities to coordinate Federal efforts and develop Federal policy on prudential aspects of international insurance matters. The Director stated that FIO follows the authorities outlined in Dodd-Frank, IAIS By-Laws, IAIS Members Handbook, and Treasury policies and procedures. We reviewed these materials and concluded that they provide comprehensive guidance to FIO in carrying out its activities related to international insurance matters.

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## IAIS Activities

In October 2011, FIO joined the IAIS to represent the United States internationally as provided by Dodd-Frank, and since then, was actively involved in the development of the global basic capital requirements. The FIO Director explained that FIO's role in the implementation process of the global capital requirements is aimed to promote standards that can be adopted in a consistent manner by the FRB and State insurance regulators. Each State insurance regulator will decide if implementation is practical for their jurisdiction and if so, how best to implement the standards in their State. Once the standards are developed, they will be tested to determine their practicality and value. If needed, standards will be refined and re-calibrated. The FIO Director went on to say that ultimately, each State insurance regulator has the authority to tailor the global capital requirements as is prudent for the respective State's jurisdiction.

FIO spent the first several months of its membership gaining an understanding of the IAIS' internal processes and building relationships. Over the course of 2012, FIO increased its IAIS participation as the office continued to develop and grow. FIO represents the United States on the IAIS Executive Committee, two steering committees (the Technical Committee and the Financial Stability Committee), two task forces (the Strategy Task Force and the Global Systemically Important Insurers (G-SII) Methodology<sup>4</sup> Task Force), and many subcommittees. The FIO Director was appointed Chairman of the Technical Committee in October 2012 and was reappointed in October 2014. In January 2015, the FIO Director was appointed as Chairman of the G-SII Methodology Task Force and other FIO officials served in various capacities such as Chairman of the Financial Crime Task Force and Vice Chairman of the Field Testing Working Group.

FIO has worked on the development of the global basic capital requirements for G-SII with the IAIS. This initiative is a three step

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<sup>4</sup> The IAIS developed an assessment methodology to identify insurance-dominated financial conglomerates whose distress or disorderly failure, because of their size, complexity, and interconnectedness, would cause significant disruption to the global financial system and economic activity.

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process. The first step is to develop basic capital requirements. The second step is to develop higher loss absorbency requirements to apply to G-SIIs, which is due to be completed by the end of 2015. The third is to develop a risk-based, group-wide global insurance capital standard, due to be completed by the end of 2016, with refinement and final calibration taking place in 2017 and 2018, and to be applied to internationally active insurance groups<sup>5</sup> by 2019.

### **Consultation and Coordination with State Regulators**

FIO regularly communicated with State insurance regulators on insurance matters of national and international importance as authorized by Dodd-Frank. The FIO Director told us that FIO has regular communication with NAIC members (e.g. State insurance regulators) through scheduled and ad hoc calls and meetings, IAIS committee level meetings, IAIS conferences, and NAIC membership meetings, upon request. As members of these IAIS committees and conferences, they engage in formal and informal teleconferences and follow-up meetings as well as the regularly scheduled meetings. The FIO Director said that most of the communication occurs via teleconference and usually monthly but this can increase depending on the urgency of the topic. Also, the FIO Director is occasionally invited to address the NAIC membership to discuss a specific topic.

We interviewed the State insurance commissioners for: California, Connecticut, Florida, Illinois, Minnesota, Montana, New Jersey, New York, Pennsylvania, and Tennessee. The interviewed State insurance commissioners included the current president of the NAIC, and represented a cross-cut of States, including States that were home to some of the largest U.S. insurance companies. Some State insurance commissioners we interviewed stated the communications were adequate; other commissioners suggested that a consistent, well-defined, transparent consultation process would be more effective. Such a process should encourage dialogue and solicit and consider input from State regulators on insurance matters affecting the States as well as promote transparency.

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<sup>5</sup> The NAIC defines an internationally active insurance group as a large internationally active group that includes at least one sizeable insurance entity.

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Dodd-Frank provides that FIO has the authority to “consult with the States (including State insurance regulators) regarding insurance matters of national importance and prudential insurance matters of international importance.” Through our interviews with the State insurance commissioners, we learned that FIO consulted or periodically shared information with the States on insurance matters. In this regard, FIO disseminated information from the IAIS, through formal and informal meetings with State representatives, and collaborated on insurance topics discussed at the IAIS. Some of the commissioners interviewed considered the communications appropriate and unrestricted, but suggested areas of improvement. Specifically, the commissioners suggested FIO have (1) direct consultation with the States on a regional basis to overcome the hurdle of consulting with States individually, (2) more timely communication of information, and (3) a designated FIO point of contact. Other commissioners considered the process as non-existent or somewhat limited due to what they viewed as the inconsistent nature of the communications, lack of transparency in FIO’s processes, and lack of feedback on final decisions made by FIO and the IAIS.

FIO is not the only entity providing insurance related information to the State insurance regulators. We learned from the State insurance commissioners that they also receive information from FRB, NAIC, the IAIS, The Geneva Association,<sup>6</sup> other State regulators, and the insurance industry, both nationally and internationally. The commissioners told us that the information sharing process was not perfect, oftentimes constrained by timing requirements imposed by the IAIS which limits their ability to provide comprehensive, collaborative input to FIO.

We note that Dodd-Frank does not establish guidelines or expectations on how FIO may exercise its authority to consult with State insurance regulators. However, we believe the development of a consistent, transparent, comprehensive consultation process would facilitate a process that promulgates one of the intended purposes of this provision of the law.

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<sup>6</sup> The Geneva Association, founded in 1973 by global insurers, is an international insurance think tank that produces and distributes research and analysis on global strategic insurance and risk management issues.

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It should also be noted that certain Members of Congress have expressed concern with the accountability and transparency of international insurance discussions. In this regard, S.1086, the International Insurance Capital Standards Accountability Act, was introduced on April 27, 2015, that would among other things, have the Secretary of the Treasury, FRB, and FIO achieve consensus positions with State insurance regulators. While the fate of this legislation is unknown at this time, it does indicate the relevance of consultation with State insurance regulators.

## **Recommendation**

We recommend that the FIO Director ensure FIO continues to build on the consultation process with the State insurance regulators to promote more consistent communication, timely dissemination of information, consideration of solicited feedback, and increased transparency of FIO's activities relating to the IAIS.

### Management Response

Management agreed with the recommendation. FIO will build on its existing consultation process with State insurance regulators in the ways outlined in this report. FIO welcomes additional ways to enhance its existing regular collaboration with State insurance regulators and FRB, and will take steps to implement the report's recommendation.

### OIG Comment

Management's commitment to enhance its consultation process is responsive to our recommendation. FIO will need to record the estimated date for completing its planned corrective actions in JAMES.

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We appreciate the courtesies and cooperation provided to our staff during the audit. If you wish to discuss the report, you may contact me at (202) 927-0384 or Andrew Morgan, Audit Manager, at (202) 927-8121. Major contributors to this report are listed in appendix 3.

Jeffrey Dye /s/  
Director, Banking Audits

The objectives of this audit were to (1) identify the authority(s) and processes by which the Department of the Treasury (Treasury), through the Federal Insurance Office (FIO), coordinated Federal efforts and developed Federal policy on prudential aspects of international insurance matters, including representing the United States, as appropriate, in the International Association of Insurance Supervisors (IAIS) and (2) determine whether Treasury's activities, through FIO, were consistent with its authority(s) and whether such activities were appropriately informed by consultation with the States, including State insurance regulators.

To accomplish these objectives, we reviewed the following:

- the Dodd-Frank Wall Street Reform and Consumer Protection Act
- a prior Office of Inspector General Report titled *Treasury Made Progress To Stand Up the Federal Insurance Office, But Missed Reporting Deadlines* (Report No. OIG-14-036; issued May 14, 2014)
- a selection of available documentation from FIO regarding its IAIS activities. The documentation reviewed included meeting agendas, meeting minutes, speeches by the FIO Director, summary records (e.g., documents discussed during the meeting), and action points (e.g., tasks assigned to meeting participants as a result of discussions).

We also interviewed the following officials:

- the FIO Director and FIO Deputy Director to obtain a broad overview of FIO's work with the IAIS.
- the State insurance commissioners for California, Connecticut, Florida, Illinois, Minnesota, Montana, New Jersey, New York, Pennsylvania, and Tennessee to gain an understanding of FIO's efforts to consult with State insurance regulators. We selected five commissioners based on their level of participation in IAIS (from very active to relatively inactive) (California, Florida, New York, Pennsylvania, and Tennessee). Four commissioners interviewed were selected to provide coverage of those States

where the largest insurance companies are domiciled for the health, property and casual, and life insurance markets (Connecticut, Illinois, Minnesota, and New Jersey). Additionally, we interviewed the current President of the National Association of Insurance Commissioners, who is the commissioner for Montana.

We performed our audit field work from October 2014 through March 2015.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix 2  
Management Comments



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

May 14, 2015

Mr. Jeffrey Dye  
Director, Banking Audits  
Officer of Inspector General  
Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Washington, DC 20220

Dear Mr. Dye:

This letter responds to the draft audit report (Draft) regarding the Federal Insurance Office's (FIO) participation in the International Association of Insurance Supervisors (IAIS) and FIO's consultation process with State insurance regulators. FIO appreciates your office's work over the course of the audit and values your feedback on these important issues. This letter provides FIO's official comment and reply to the Draft, supplementing earlier technical comments.

Title V of the Dodd-Frank Wall Street Reform and Consumer Protection Act authorizes FIO "to coordinate Federal efforts and develop Federal policy on prudential aspects of international insurance matters, including representing the United States, as appropriate, in the [IAIS]." Separately, FIO is authorized "to consult with the States (including State insurance regulators) regarding insurance matters of national importance and prudential insurance matters of international importance."

We are pleased that the Draft finds that FIO engaged in multiple activities when performing its function as the representative for the United States in the IAIS, including serving in IAIS leadership positions, actively participating in IAIS conferences, and regularly communicating with State insurance regulators on international insurance matters. We also appreciate that the Draft concludes that, in a variety of formal and informal ways, FIO regularly communicated with State insurance regulators on matters of national and international importance.

We agree with the Draft's recommendation that FIO build on its existing consultation process with State insurance regulators in the ways outlined in the Draft. FIO welcomes additional ways to enhance its existing regular collaboration with State insurance regulators and the Board of Governors of the Federal Reserve System, and will take steps to implement the Draft's recommendation.

Thank you for your office's work on the Draft. We look forward to working with your office in the future.

Sincerely,

A handwritten signature in blue ink, appearing to read "Michael T. McRaith".

Michael T. McRaith  
Director, Federal Insurance Office

Appendix 3  
Major Contributors To This Report

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Andrew Morgan, Audit Manager  
Vicki Preston, Auditor-in-Charge  
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**Department of the Treasury**

Deputy Secretary  
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OIG Budget Examiner

**United States Senate**

Chairman and Ranking Member  
Committee on Appropriations

Chairman and Ranking Member  
Subcommittee on Financial Services and General Government  
Committee on Appropriations

Chairman and Ranking Member  
Committee on Banking, Housing, and Urban Affairs

**U.S. House of Representatives**

Chairman and Ranking Member  
Committee on Appropriations

Chairman and Ranking Member  
Subcommittee on Financial Services and General Government  
Committee on Appropriations

Chairman and Ranking Member  
Committee on Financial Services